VOLUNTARY DISCLOSURE NARRATIVE: REPORTING CONTENT, STAKEHOLDERS, EXTERNAL MATERIALITY AND USEFULNESS.

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VOLUNTARY DISCLOSURE NARRATIVE: REPORTING CONTENT, STAKEHOLDERS, EXTERNAL MATERIALITY AND USEFULNESS.

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Abstract

This PhD by published work comprises 11 papers published between 2006 and 2009. The research is focussed upon voluntary and related financial reporting by UK companies in their annual report. The level, and more importantly, the importance of voluntary disclosure has significantly increased over the last 20 years (Campbell, Moore and Shrives, 2006) and this submission provides academic and policy relevant contributions to that field. The papers make specific contributions to the extant literature in discrete areas primarily; philanthropy, social and environmental reporting.

These 11 publications adopt a range of research methods appropriate to different research questions. The qualitative papers demonstrate successful engagement with a number of high level participant stakeholders from the building society sector, fair trade organisations and UK capital markets as well as capturing disclosure content relevant to other stakeholder groups. Other papers have adopted a positivist approach with appropriate longitudinal and cross sectional data used to test theory. Two of the research projects relating to strategic philanthropy and decision–usefulness of disclosure were supported by external research funding and therefore demonstrate the policy relevance and impact of the research contribution in those areas.

Within the commentary, the research is presented in two sections, followed by a conclusion which shows the research impact of the publications and the international dissemination of the research contribution and findings. The key findings of Section 1 show the financial and non-financial influences on levels of philanthropy; inconsistency of philanthropy policy reporting; social disclosure responses to legitimacy threats and the reporting validity of the annual report; a holistic approach to responsible business practice and insights into the mainstreaming of Fair Trade. Section 2 provides findings into the decision-usefulness of a range of voluntary disclosure narratives in the annual report, developed in detail in respect of environmental disclosures and related risk factors and insights into the current issues facing accounting.

Keywords: Disclosure, philanthropy, social and environmental reporting, decision-usefulness, stakeholders.

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Acknowledgments

I owe thanks to my family, friends and colleagues for their continuous support of my PhD by published work. Whilst the published work is recorded from 2006, the research process began around 2002-03. At that time I was encouraged by both David Campbell and Philip Shrives. It was at the Financial Reporting and Business Communication conference in Cardiff in July 2003, that I appreciated the challenges and the pleasure of research as an endeavour, and also the opportunities it provides to forge new working partnerships. To David and Philip, my thanks to you both for your support and true friendship.

I have been fortunate to be able to enjoy researching with others and I thank all of those colleagues who I have collaborated with over the last seven years. As well as David and Philip, I also thank Geoff Moore, Jane Gibbon and more recently Mike Jones, the latter in particular, for his sage advice and friendship over recent years.

Solitude provides for reflection alongside the noise of collaboration and friendship. I find this and the freedom to think with clarity in places that are now part of me: Hesket-New-Market; The Old Crown and the Lakeland Fells. It is right that this trio are acknowledged for the time I spend within them and it is my desire one day to make that time permanent.

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Finally, I owe my thanks to my family, especially to my wife, Marie, and daughter, Emma. Their love and support are unstinting, enabling me to enjoy my research and it is to them that this PhD is dedicated.

Declaration

I declare that no outputs submitted for this degree have been submitted for a research degree of any other institution.

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1. Publications submitted for PhD by published work.

Paper 1: Campbell, D. and Slack, R. (2006) ‘Public visibility as a determinant of the rate of corporate charitable donations’,
Business Ethics: A European Review, January 2006, Volume 15, Number 1, pp. 19-28.
Joint author

Paper 2: Moore, G., Gibbon, J. and Slack, R. (2006) ‘The mainstreaming of Fair Trade: a macromarketing perspective’,
J*ournal of Strategic Marketing*, December 2006, Volume 14, Number 4, pp. 329-352.
Minor contributing author

Paper 3: Campbell, D. and Slack, R. (2007) ‘The influence of mutual status on rates of corporate charitable contributions’,
Journal of Business Ethics, August 2007, Volume 74, Number 2, pp. 191-200.
Principal author

Paper 4: Campbell, D. and Slack, R. (2007), ‘The strategic use of corporate philanthropy: building societies and demutualisation defences’,
Business Ethics: A European Review, October 2007, Volume 16, Number 4, pp. 326-343.
Principal author

Paper 5: Slack, R. (2008), ‘Employee involvement in corporate philanthropy: informing company policy, reputation management and employee motivation’, *The 9th International Conference on Human Resource Development Research and Practice Across Europe*, Lille, France, refereed conference paper proceedings, ISBN 2-9516606-9-3, May 2008.
Sole author

Paper 6: Campbell, D. and Slack, R. (2008) ‘Corporate “philanthropy strategy” and “strategic philanthropy”: some insights from voluntary disclosures in annual reports’,
Business and Society, June 2008, Volume 47, Number 2, pp. 187-212.
Principal author

Paper 7: Slack, R. and Shrives, P. (2008) ‘Social disclosure and legitimacy in Premier League football clubs: the first ten years’,
Journal of Applied Accounting Research, June 2008, Volume 9, Number 1, pp. 17-28.
Joint author

Paper 8: Moore, G., Slack, R. and Gibbon, J. (2009), ‘Criteria for Responsible Business Practice in SMEs: an exploratory case of U.K. Fair Trade organisations’,
Journal of Business Ethics, October 2009, Volume 89, Number 2, pp. 173-188.
Joint author

Paper 9: Campbell, D. and Slack, R. (2008), *Social and Environmental Narrative Reporting: Analysts’ Perceptions*, The Association of Chartered Certified Accountants (ACCA), London, Research Summary Report re Research Report 104.
Principal author

Publications submitted for PhD by published work (continued).

Paper 10: Campbell, D. and Slack, R. (2008), *Narrative Reporting: Analysts' Perceptions of its Value and Relevance*, The Association of Chartered Certified Accountants (ACCA) Research Monograph, Research Report 104.
Joint author

Paper 11: Jones, M. and Slack, R. (2009), *The Future of Financial Reporting 2008: Measurement and Stakeholders*, The Association of Chartered Certified Accountants (ACCA), London, Published Discussion Paper.
Joint author

All declarations of co-authorship of published work are confirmed in Appendix 1

Included in commentary and noted as Appendix 2

Campbell, D., McPhail, K. and Slack, R. (2009) 'Face work in annual reports: a study of the management of encounter through annual reports, informed by Levinas and Bauman', *Accounting, Auditing & Accountability Journal*,
September 2009, Volume 22, Number 6, pp. 907-932.

2. Commentary on PhD by published work.

Voluntary disclosure narrative: reporting content, stakeholders, external materiality and usefulness.

Introduction

This PhD by published work commentary comprises three sections. Sections 1 and 2 set out the author's research contribution and this is followed by its academic and practice impact in Section 3. The published work on which this submission is based is shown on pages 1 and 2. Disclosure forms the focus of the work with contributions to a number of discrete reporting areas with regard to content, stakeholder engagement and decision-usefulness.

Section 1 summarises and presents the first eight papers, of which the first four formed the author's inclusion in Northumbria University's Business and Management submission to the RAE 2008. Section 2 summarises and presents three further papers (papers 9 to 11), published as research monographs and discussion papers[1].

Within Section 1, Papers 1, and 3 to 6 focus on corporate philanthropy, providing contributions to our understanding of the influences on levels and patterns of philanthropy and related reporting. Philanthropy is, in part, a measure of corporate social performance and Paper 7, more generally, develops social reporting within a legitimacy framework. Papers 2 and 8 focus on social responsibility and related reporting and these two papers additionally make contributions to the developing Fair Trade literature.

Section 2 focuses on the decision-usefulness of voluntary disclosures and provides discussion and contribution to the current debates in accounting research. Paper 10 is the basis of the research contribution regarding decision-usefulness of voluntary disclosure with Paper 9 making a specific contribution on the decision-usefulness of environmental disclosure. Paper 11 sets out a forum for current debate in accounting and provides original commentary on a range of issues that currently challenge both the accounting profession and academics.

[1] This commentary summarises the key research contributions of the published work they contain but is necessarily limited in its scope in compliance with Northumbria University PhD by Published Work regulations stipulating a 5000 word commentary. The detailed discussions within the research are presented in the submitted papers.

Section 1: Voluntary disclosure narrative: reporting content and stakeholders.

The first discrete area of disclosure to which research contribution has been made is corporate philanthropy. Philanthropy disclosure enables reporting companies to demonstrate and signal social responsibility through philanthropy policy and narrative reporting and provides a research opportunity to examine influences towards their levels of giving. Papers 1, 3 and 4 report discrete influences on levels of philanthropy. Papers 5 and 6 examine philanthropy disclosure and their contribution to our understanding of philanthropy policy reporting.

The extant philanthropy literature had identified a number of influences on levels of giving which are summarised in Table 1 below.

Table 1: Influences on charitable donations

Influences on levels of charitable donations	**Authors**
Firm Size	Brammer and Millington (2004) Seifert, Morris and Bartkus (2003) Buchholtz, Amason and Rutherford (1999) Useem (1988)
Levels of profit and gearing	Brammer and Millington (2005a) Adams and Hardwick (1998)
Industry sector	Brammer and Millington (2003) Cowton (1987)
Levels of cash-flow	Seifert, Morris and Bartkus (2004)
Board composition and ethnicity	Williams (2003) Edmondson and Carroll (1999) Wang and Coffey (1992)

Of the identified influences on giving, firm size, measured by market value, and level of profit were found to be statistically significant (at the 1% level) by the findings reported in Paper 5 confirming previous research. Paper 1 contributes to the extant literature on the influences on giving, examining firm visibility. Firm size has been conflated with visibility as subsequently noted by Gan (2006) and Brammer and Millington (2006) and evidenced in prior research, see for instance Brammer and Millington (2004), Seifert, Morris and Bartkus (2004) and Adams and Hardwick (1998). Visibility as an influence on philanthropy was simultaneously addressed (*Business Ethics: A European Review*, 2006 15/1) by Paper 1 and Brammer and Millington, the latter claiming that the main contribution of their paper was a 'systematic analysis of corporate philanthropic expenditures that controls for firm size and visibility' (Brammer and Millington, 2006, p.7). Whilst their research finds a positive relationship between organisational visibility and level of giving, the research uses media hits/coverage as a proxy for company visibility and the financial data is drawn from one year, 2001, and consequently there are no longitudinal findings. Paper 1 contends that financial reporting and city news as a proxy may not indicate public visibility to a *wider* stakeholder base. Accordingly, Paper 1 measured visibility through public recognition (and see Clarke and Gibson-Sweet, 1999) finding a statistically significant positive relationship between visibility and levels of giving using a 15 year longitudinal dataset. The use of public recognition is a refinement of the proximity to end user research method (Clarke and Gibson-Sweet, 1999) and the visibility influence contribution is cited in later research (Zhang, Rezaee and Zhu, 2009, Zhang *et al.*, 2009 and van Nimwegen *et al*., 2008). The findings, together with Paper 5 concerning employees in philanthropy, provide a theoretical contribution consistent with a resource based view of the firm (Barney 1991) where giving enhances a unique firm resource, namely reputation or image consistent with Seifert, Morris and Bartkus (2004).

If more visible companies manage greater pressure from stakeholders (Meznar and Nigh, 1995 and Erfle and McMillan, 1990) and enhance stakeholder reputation and accountability, the established link of visibility to giving shown by Paper 1 is an important contribution. This re-affirms Brammer and Millington (2005b), Saiia, Carroll and Buchholtz (2003) and Fombrun and Shanley (1990) that higher levels of philanthropy are positively associated with reputation. Subsequent to Paper 1, Gan (2006), found a similar positive relationship between levels of public scrutiny (again measured by press releases) and philanthropy.

Papers 3 and 4 contribute to the extant literature by applying philanthropy research in a sector specific context and examine ownership as an influence on giving. Paper 3 examined, through a 14 year longitudinal cross sector study (1990-2003) the claims, such as those of the Building Society Association (BSA), that building societies' mutual status and community orientation results in more generous giving than that of the banks.

Paper 3 examined giving rates for 31 building societies, seven high street publicly listed banks and five building society conversions over this period. It found no convincing support for the claims that building societies are structurally more generous than banks, refuting claims of such generosity, although the research showed a pronounced shift in building society giving in the period 1996-1998. These findings are extended in Paper 4 which demonstrates the strategic use of philanthropy by building societies in support of their social positioning in the context of the demutualisation debate.

Public awareness of demutualisation was based on a broad based media hits approach consistent with the media agenda literature (see for instance Deegan, Rankin and Tobin, 2002). Change in legal form and its public awareness had not been previously examined as an influence on philanthropy and provides evidence to contend Adams and Hardwick's (1998, p.641) conclusion of 'no support for the view that there is a link between discretionary donations and a company's ownership structure'. Paper 4 provides evidence of the influence of ownership structure and giving. It examines a strategic change in giving by building societies relevant to their mutual ownership structure to support their claims of local community involvement. This paper also provides contribution to the demutualisation literature, complementing its extant economic (Heffernan, 2005 and Tayler, 2003) and social (Michie and Blay, 2004 and Lewin, 2002, Clarke, 1998) bases. The findings in Paper 4 confirm a strategic shift in charitable giving by building societies in order to support their claims of mutuality and demonstrate the use of philanthropy in societal positioning, and as cited by Spence and Thomson (2009) through the creation of moral capital. Papers 3 and 4 illustrate the institutional shift towards giving rates across the remaining mutual societies, who faced demutualisation pressure in part due to the heightened media coverage. This shift and societal positioning is consistent with the notion of impact philanthropy (Duncan, 2004).

As discussed earlier, philanthropy is recognised in the extant literature contributing to company reputation and social positioning with stakeholders and consistent with these motivations, (evident in Paper 4) there has been increased use of strategic philanthropy (McKinsey, 2008; Brammer, Millington and Pavelin, 2006; Ricks and Williams, 2005; Saiia, Carroll, and Buchholtz, 2003 and Porter and Kramer, 2002). Papers 5 and 6 contribute to the strategic philanthropy literature through their examination of philanthropy policy disclosure and also (specifically for Paper 5) the involvement of employees (and see Ricks and Williams, 2005 and Adams and Hardwick, 1998). Consistent and clear policy reporting enable increased accountability of philanthropy to relevant stakeholders and provide additional transparency of information. Post and Waddock (1995) had differentiated between strategic philanthropy and philanthropy strategy.

Papers 5 and 6 specifically contribute to this by their reporting of disclosure resolved at those levels. Paper 6 (cited by Crane and Kazmi, 2010 and Rumsey and White, 2009) is the first paper to give a longitudinal insight into philanthropy policy disclosure and responds to Seifert, Morris and Bartkus (2004) and Adams and Hardwick's (1998) calls for longitudinal studies. Paper 6 provides evidence over a 15 year period (1998-2002), along with cross sectional data for 2002 and shows a general increase in policy disclosure over time, although this is both inconsistent within companies and patchy between them. The most common policy areas cited relate to identified priority areas and local community support, consistent with reputation and stakeholder management. Paper 5 presents a similar finding of key policy areas testing a later time period (2006). Overall, however, the findings in Papers 5 and 6 show that external disclosure of strategic intent are not fully evident across all companies. This highlights potential accountability and transparency concerns regarding the usefulness of philanthropy disclosure.

As well as capturing policy disclosure, Paper 5 specifically examines disclosure towards employees and philanthropy. This contribution has significance within a resource based view of the firm, that increased employee involvement in philanthropy will promote enhanced teamwork and morale and a resource dependence view of increased employee loyalty, recruitment and retention (Barney 1991). Levels of recruitment and retention were specific benefits of philanthropy reported by McKinsey (2008). As a contribution to practice, Paper 5 shows that whilst employees are reported as being involved in philanthropy, evidenced by narrative and pictorial representation, they are far less recognised with regard to policy involvement or its reporting. The use of pictorial images, including employees, in annual reports is more fully developed by Campbell, McPhail and Slack (2009) (Appendix 2) and the author has externally examined (January 2010) a doctoral thesis on image reporting in annual reports. The findings in both Papers 5 and 6 illustrate the greater use of narrative in reporting rather than actual policy intent consistent with Spence and Thomson (2009).

Paper 7 provides a sector specific study of social disclosures contributing to the extant social disclosure literature and to the relatively small literature on football clubs in accounting research. Previously, Morrow (2005) and McGuire and Fenoglio (2004) had examined image management of football clubs. For a review of Morrow (2005) by the author, published in *British Accounting Review* (2006) see Appendix 3. Paper 7 examines social disclosures, in a legitimacy framework, made in response to adverse press reports. It uses content analysis to examine relevant disclosures, a research method replicated in papers 2, 5, 6 and 8 (see Krippendorff, 2004) and discussed further by Linsley and Slack (2009).

Media hits were used in Paper 7 to determine the extent of adverse and positive comment that related to Premier League football over the ten year period 1993 to 2002. Media Agenda Setting Theory (MAST) applied to the increase of adverse reporting would predict an increased community concern (Deegan and Unerman, 2006 and Brown and Deegan, 1998), consistent with a consequent legitimacy issue (Deegan, Rankin and Tobin, 2002). In the extant literature much of the focus had been on environmental legitimacy issues and reporting, see for instance Deegan, Rankin and Voght (2000), O'Donovan (1999), Deegan and Gordon (1996) and Patten (1992). This paper contributes to social disclosure application of legitimacy theory and Lindblom's (1994) legitimation strategies. Legitimacy theory (along with impression management) is used by Jones and Slack (2010a) concerning the disclosure of environmental targets.

Paper 7 also contributes to the use in accounting disclosure research of the annual report as a reporting vehicle to stakeholders. The extant literature presumes that managers use annual report disclosures to respond to legitimacy threats, see for instance Deegan, Rankin and Tobin (2002) where O'Donovan (1999) is cited to provide justification of this approach. Paper 7 confirms O'Donovan (1999) on the use and importance of the annual report by management to inform stakeholders about community activities.

Philanthropy and social reporting are subsets within corporate social responsibility. Paper 8, in its examination of responsible business practice (RBP) is, within the accounting ethics literature, the first paper to establish a holistic criterion based evaluation applicable to RBP, covering governance, employees, external stakeholders and reporting (the latter including social reporting covered by Paper 7). This research responds to one of the calls for research contributions from the 2005 EABIS conference, 'SMEs and CSR: identifying knowledge gaps' (Durham University, December, 2005) reported by Moore and Spence (2006). The extant literature had hitherto confined analysis to more specific areas of RBP.

Within Paper 8, the derived RBP criteria were tested against UK Fair Trade organisations. The findings show that whilst there was some evidence of RBP reporting by them, this was not comprehensive despite their broader objective of influencing the mainstream discussed in

Paper 2. Such a finding is consistent with the extant literature examining more general RBP related disclosure by SMEs (Jenkins, 2006 and Murillo and Lozano, 2006), although previously untested in a Fair Trade context, and presents a challenge to practice within Fair Trade and more generally for the noted lack of RBP disclosure 'champions'. Fair Trade was chosen for two reasons, firstly due to the social remit of Fair Trade itself and secondly to develop further contribution to the Fair Trade literature.

Some of the challenges to the mainstreaming of Fair Trade had previously been examined in Paper 2. Low and Davenport (2006), Kilbourne (2004) and Dolan (2002) had raised questions concerning the dominant social paradigm (DSP) and the challenges to this, either from within or without of the current economic system. Within Paper 2, Fair Trade was explicitly recognised by the major supermarkets (e.g. Sainsbury's and Tesco) as forming *part* of their overall commitment to CSR. The paper gained its insights, and contribution, into Fair Trade organisations and supermarkets through interviews with senior management supported by content analysis of websites. Despite the complex of Fair Trade characteristics (Lancaster 1966), from the supermarket perspective, Paper 2 found evidence of uniformity regarding the Fair Trade definition, although the emphasis was towards the consumer rather than supply chain and sourcing, those being more addressed by Ethical Trading Initiative (ETI). Further, Paper 2 provided a contribution reporting on the disparity of views held by the supermarkets toward Fair Trade mainstreaming and the consequent challenges still faced by the macromarketing literature for alternatives to DSP.

Section 2: Voluntary disclosure narrative: stakeholders, external materiality and decision-usefulness

Paper 10 contributes to the literature into the decision-usefulness and materiality of a range of voluntary disclosure categories namely; the chairman's statement; risk; corporate governance; social and environmental reporting. The research responds to Smith (2004), Dierkes and Antal (1985) and specifically to Lui, Markov and Tamayo (2007) and Robb, Single and Zarzeski (2001) to address decision-usefulness of voluntary disclosures to analysts. The research focussed on the views of sell-side analysts, a key stakeholder group (Johannson, 2007 and Fogarty and Rogers, 2005). Paper 10 provides a unique contribution to the voluntary disclosure literature by its consideration of the decision-usefulness of the whole of the 'front end' of the annual report to the analyst group. All of the prior cited research examines individual components of reporting. The findings show a general lack of decision-usefulness of voluntary disclosure, although the analysts were divided in terms of its psychological value to them if it were to be removed from annual reporting. This is the first research reporting on the usefulness to a stakeholder group of the collective range of voluntary disclosure.

Conducting interviews with nineteen UK sell-side bank analysts demonstrates the level of stakeholder engagement and the consequent depth of the research findings. This is a further significant contribution of the work and consistent with Parker's (2005) call for direct researcher engagement in the field. Paper 10 provides an original contribution examining a sector specific sell-side analyst group and in doing so addresses a gap within the prior literature. Extant decision–usefulness literature involving analysts lacked sector focus (Solomon and Solomon 2006, Barker, 1998 and Day 1986) and did not distinguish sell-side analysts and buy-side analysts, such as fund managers (as discussed by Arnold and Moizer, 1984). Moreover in the earlier analyst research, Bouwman, Frishkoff and Frishkoff (1987) used graduate business students as surrogates for the analyst user group and no differentiation was made between sell-side analysts and fund managers (Chan and Milne, 1999, Milne and Chan, 1999 and Deegan and Rankin, 1997). Paper 10, by its focus on a single sector and participant group contributes to research method in disclosure studies providing a sector specific example to facilitate future research and to the extant literature in the various sub-disciplines of voluntary reporting.

For risk reporting, extant literature had generally found that disclosures lacked cohesiveness, were often too generic and did not provide for quantifiable risk impact (Linsley, Shrives and Crumpton, 2006, Linsley and Shrives, 2006; 2005 and Woods, 2004). Consistent with this research from a reporting stance, Paper 10 contributes to risk reporting from a user perspective, namely that sell-side analysts did not value risk reporting due to its lack of specificity and hence relevance and their perception of boiler-plating. Their views on governance reporting provide similar contribution to the corporate governance literature as well as highlighting their assumed reliance upon UK bank governance in the light of subsequent events. Paper 10 also contributes towards the understanding of the decision-usefulness of the chairman's statement. Prior research had provided mixed evidence examining the content and usefulness of the chairman's statement to stakeholders drawing on, for instance, impression management and obfuscation (Aerts, 2005, Clatworthy and Jones, 2001 and Courtis, 1998). Again, from a user perspective, Paper 10 provides a contribution, finding a lack of granularity and strategic content in reporting and consequently its relatively low usefulness to analysts as a stakeholder group.

The specific research contribution concerning environmental disclosure usefulness is marked by Paper 9. The extant academic literature shows a number of papers in support of the decision-usefulness of environmental disclosure summarised in Table 2 below.

Table 2: Decision-usefulness of environmental disclosure.

Decision-usefulness of environmental disclosures relating to:	**Authors**
Analysts, fund managers and institutional investors	Aerts, Cormier and Magnan, (2008) Holm and Rikhardsson (2008) Solomon and Solomon (2006) Deegan (2004) Miles, Hammond and Friedman (2002)
Bank lending decisions	Aintablian, McGraw and Roberts (2007) Thompson and Cowton (2004) Thompson (1998)
Company stakeholders and investors	Cho and Patten (2007) Cormier, Magnan and van Velthoven, (2005) Lee and Hutchison (2005)
Financial performance and share price	Murray *et al.* (2006) Richardson, Welker and Hutchinson (1999)

In contrast to these, there are a number of papers that have argued against the usefulness of such disclosures to analysts, namely; Chan and Milne (1999), Milne and Chan (1999), Deegan and Rankin (1997) and Business in the Environment (1994). Paper 9 provides clear findings for a specific analyst group, sell-side bank analysts. This paper found a general dismissal of its usefulness and materiality (cited by Kuruppu and Milne, 2010 and Rowbottom and Lymer, 2009) and also their general lack of interest in environmental reporting. Further, the analysts dismissed any link of environmental risk, disclosure and bank lending, a finding inconsistent with the prior research of Thompson and Cowton (2004) who found that banks themselves valued corporate environmental disclosure as part of their risk filter.

Juravle and Lewis (2008) examined the organizational and institutional impediments that exist to the mainstreaming of socially responsible investment (SRI) that includes environmental considerations. From an organizational perspective, (Davis, Lukomnik and

Pitt-Watson, 2006), they argued mainstream analysts are poorly incentivized to move beyond short term financial performance. The findings of Papers 9 and 10 support this organizational impediment argument. Additionally, the findings contribute to the literature on the conflict between personal and professional values (Milne and Chan, 1999 and Dierkes and Antal, 1985).

Beattie and Pratt (2002) set out some of the key challenges that face financial reporting, in particular voluntary disclosure including the decision-usefulness of reporting and the varying needs of primary users. Their research analysed the views of four user groups including expert users, for instance analysts. Whilst Papers 9 and 10 examined decision-usefulness, it was limited to one expert group and considered voluntary reporting only, although it was evident that statutory financial information was most material to their needs. To widen the context of discussion and contribution relevant to financial reporting, Paper 11 provides policy relevant discussion and commentary encapsulating decision-usefulness, the conceptual framework, stakeholder communication, the use of Fair Value and accounting measurement; the latter forming a special issue of *European Accounting Review*. McInnes, Beattie and Pierpoint (2007) is one of the papers discussed in Paper 11 and recognises the need for decision-usefulness of information to a range of stakeholders, a critical contribution to which is provided by Papers 9 and 10.

Paper 11 is published as a Discussion Paper by ACCA and was informed by five presentations extensively commented on by the author. It provides applied discussion and focus for policy relevant debate between senior accounting practitioners, accounting standard setters and accounting academics. The presentations included, Richard Martin (Head of Financial Reporting, ACCA), Neil Chisman (former finance director of Stakis plc and former member of the Financial Reporting Council) and professors McInnes, Whittington and Macve, the latter two having standard setting board experience. Whilst there is a considerable literature base on the issues discussed by Paper 11, summarised in Table 3, this enables a contemporary and practice informed critique and discussion of these areas.

Table 3: Indicative literature on contemporary accounting issues

Contemporary accounting issues	**Authors**
Accounting measurement	*Accounting and Business Research, Special Issue, International Accounting Policy Forum* (2007) Barth (2007) Ohlson (2006)
Fair Value	Laux and Leuz (2009) Véron (2008) Penman (2007)
Conceptual framework	Laughlin (2008) Whittington (2008)
Stakeholder dialogue	McInnes, Beattie and Pierpoint (2007) Unerman and Bennett (2004)

Subsequent to Paper 11, a second Discussion Paper by Jones and Slack (2010b) was published '*The Future of Financial Reporting 2009: A Time of Global Financial Crisis*' (and also see Ryan 2008) and a further symposium held (8 January 2010, London). Both of these, consistent with Paper 11, involved contributions from leading accounting practitioners, international standard setters and academics to which an informed commentary and discussion was developed by the authors providing an informed historic record of the challenges in accounting.

Section 3: Conclusion and research impact

Sections 1 and 2 demonstrate the research contribution of this submission for PhD by published work. The focus of the research is voluntary disclosure narrative in accounting, and the research has made contributions regarding its content, reporting, related stakeholder engagement and decision-usefulness. In doing so, the research has contributed to a number of discrete disclosure areas primarily, corporate philanthropy; social and environmental disclosure and related responsible business practice reporting. The relevance and importance of voluntary narrative research in accounting is shown by a special issue of the *Journal of Applied Accounting Research* (forthcoming 2010) examining voluntary disclosure use, users and decision-usefulness for which the author is a lead guest editor. The submission also demonstrates the use and application of a range of research methods adopted to enable contributions to the extant literature, further evidenced as an invited speaker at the British Academy of Management Research Methods Special Interest Group (March 2010).

For corporate philanthropy, the research has contributed to our understanding of the influences of the giving decision with specific contributions relevant to company visibility and ownership structure. Other influences such as company size and levels of profits were consistent with the findings in the extant literature. The research provided a sector specific contribution in its examination of UK bank and building society philanthropy and provided further contribution and a new dimension to the demutualisation literature. Significantly, this research was informed by the views of Adrian Coles, Director- General of BSA, with whom meetings were held over 2006 and 2007 and who is cited in Paper 4. Adrian, along with a former chief executive of The Mercantile Building Society, supported the successful funding application to The Nuffield Foundation (£5,000) which extended the research to interview building society directors and chief executives who held office at the time of the demutualisation debate. This has resulted in 12 subsequent interviews that have confirmed the findings of Papers 3 and 4. The research was disseminated to the BSA CSR Forum in March 2006 and it is noteworthy that ACCA Sustainability Reporting was an agenda item to which subsequent research contributed as detailed in Section 2.

The extant literature had recognised the increase in strategic philanthropy and Papers 5 and 6 contribute to our knowledge of strategic philanthropy reporting, identified priority areas in policy reporting, the involvement of employees in philanthropy and the general levels of inconsistency of policy reporting over time with consequent issues regarding philanthropy disclosure accountability and transparency. The philanthropy research contribution has enabled the author to develop research links with the Tyne and Wear Community Foundation and act as an ESRC reviewer (2007) for the Centre for Charitable Giving and Philanthropy.

The use and validity of the annual report in disclosure reporting and links to legitimacy theory were confirmed by the findings and contribution of Paper 7; important given the reliance on annual report disclosure within accounting research using legitimacy theory and related stakeholder reporting. The research provides a sector specific longitudinal contribution to the extant social reporting literature and contributes in providing a specific application of Lindblom’s (1994) legitimation strategies. For 2009, the paper was the second most downloaded full paper from the *Journal of Applied Accounting Research*. The combination of MAST and legitimacy theory is further used by the author within a research case study published in Saunders, Lewis and Thornhill (2009). The specific application of

Paper 7 to the football sector has also resulted in the author providing expert media commentary at a national level.

The wider social responsibility of business was evidenced through the contributions of Papers 2 and 8 applied to the developing Fair Trade literature. These papers provided contributions through the derivation of a holistic RBP evaluation for use within and beyond the Fair Trade literature; insights into the challenges facing change to the dominant social paradigm and the perceptions of supermarkets, as a key retail constituent, on Fair Trade and CSR. The significance of the research was evidenced by interviews carried out with senior management of UK supermarkets and with IFAT. The cross discipline recognition of the contribution to CSR and ethics research was evidenced as co-chair of the CSR and Ethics stream at the 10th International Conference on Human Resource and Development (June 2009).

Whilst Section 1 highlighted the contributions relevant to reporting content, Section 2 developed the contribution to the decision-usefulness of disclosure. The research contribution was developed through an ACCA funded research project (£13,000) providing an in depth sector specific qualitative contribution into the decision-usefulness of a range of disclosures to a key capital market stakeholder group. The extant literature had provided mixed evidence over decision-usefulness of disclosure categories, a lack of sector application and mixed usage of capital market groups in research including both sell-side and buy-side participants. The contributions of this research highlighted the lack of decision-usefulness given to voluntary disclosure overall, a unique aspect of the work due to the application of the research method. Further, it provided contributions to the literature relevant to discrete reporting areas ranging from governance and risk reporting, the chairman’s statement and social and environmental reporting. The research is policy relevant informing professional body opinion on the decision-usefulness of current voluntary narrative reporting provided by public companies and forms part of the wider discussion around the mandatory demands for narrative reporting content. The practice significance of the research was cited by Mainelli, Stevenson and Thamotheram (2009) who referred to the ‘systemic blind spot’ or lack of attention paid by sell-side analysts to the extra (non) financial performance of companies (and see Mainelli, 2009).

The contribution of Paper 10 to voluntary disclosure research is highlighted by the British Accounting Association (2008): ‘there is little research in the public domain about the consumption of voluntary disclosure and thus little is empirically known about the materiality of such disclosures.' The research was initially disseminated at a formal launch event 'Narratives– Are They Immaterial', held at the British Library, November 2008. This was hosted by Caroline Oades, ACCA Head of Research and a research panel comprising: Adrian Berendt, ACCA research committee; Dr Raj Thamotheram, Director, Responsible Investment, AXA Investment Managers; Richard Scurr, Head of Group Finance Operations, HSBC Holdings plc and Richard Thorpe, Auditing and Accounting Sector Leader and Head of Capital Adequacy Policy, Financial Services Authority. Caroline Oades said about the research:

> Delivering peer-reviewed, empirical, applied research with strong emphasis on public policy influence and practical value, ACCA's Research Programme bolsters ACCA activity in building reputation and influence among key stakeholders internationally, including members & students and their employers; governments; standard setters and regulators. Richard Slack, with a co-researcher, initiated an innovative study examining perceptions held by banking analysts towards narrative - or non-financial - reporting. ACCA supported the project from pilot, recognising Richard's insight as well as aptitude. We were well rewarded, by a project that was conducted professionally, is of high quality, receiving strongly supportive peer review comment; and is of relevance an interest to a range of stakeholders outside academia, evidenced by high turnout at each of two events promoting the study hosted by ACCA.

The event was streamed on line as part of the ACCA global website alongside a discussion forum on the research and its implications for narrative reporting and voluntary disclosure. The impact and contribution of the research is highlighted by the subsequent level of invited dissemination. This has included appearances as a key note speaker at 2008 Clear Profit symposium (held at London School of Economics) and professorial lectures and seminars at the University of Florence (November 2009) and Keele University (April 2010). The research demonstrates the effective discharge of funded research by the author, its academic impact and policy relevance.

The decision-usefulness of environmental disclosures was showcased by Paper 9 which was specifically edited for dissemination and a key note presentation at the ACCA UK Sustainability Reporting Awards (2008) to provide a mainstream sell-side perspective on decision-usefulness of social and environmental disclosures. This was hosted by Wyn Mears and Richard Aitkin-Davies, director and president of ACCA, and the respondent to the research was Emma Howard Boyd, director and head of socially responsible investment, Jupiter Asset Management, demonstrating its relevant policy and practice contribution impact. Its business relevance is further evidenced by publication in *Environmental Finance*, June 2009 (Appendix 4).

The wider contribution of the research presented in Section 2 is shown by the ACCA published Discussion Paper, demonstrating the high level of engagement of the author within accounting research at national and international levels. This represents a unique contribution in highlighting and providing informed discussion of the current debates and issues within accounting and demonstrates the link and relevance of research between accounting academics, the accounting profession, accounting professional bodies and standard setters. Its contribution is noted by Richard Martin (ACCA) in his foreword to the 2009 Discussion Paper: ‘the papers and discussion, well captured in this summary, set out the main thoughts at that point, both on the role of accounting in the crisis and the impact of the crisis on accounting…..it is very helpful to bring together accounting academics and those in the profession to consider these sorts of issues’.

Based on the contributions highlighted in Section 2, the author was invited as a professorial panel member to the American Accounting Association mid-year conference, January 2010, presenting on the current challenges and research opportunities within accounting from a UK/European perspective. This was responded to from an American accounting perspective by Professor Mark Lang (Thomas W. Hudson, Jr./Deloitte and Touche L.L.P. Distinguished Professor of Accounting) and contextualises the trends in the development of financial accounting (see also Baker and Barbu, 2007 and Arnold, 2009) and disclosure research.

Publication 1

Campbell, D. and Slack, R. (2006) ‘Public visibility as a determinant of the rate of corporate charitable donations’, *Business Ethics: A European Review*, 15(1), pp. 19-28.

Executive summaries

Firm size, organizational visibility and corporate philanthropy: an empirical analysis Stephen Brammer and Andrew Millington

This paper investigates the influence of organizational visibility, firm size and industry on corporate philanthropic expenditures within a sample of over 300 UK corporations. The study disentangles the relationships between philanthropy and firm visibility, size and industry, in more detail than has been attempted in earlier studies. Consistent with earlier studies, our findings suggest that, on average, larger firms give more to charity. However, the magnitude of the effect of size on philanthropy is, once visibility has been controlled for, roughly half the size of the effect identified in earlier studies. At the same time, we find strong support for a positive relationship between visibility and philanthropy that is approximately as large as that between size and philanthropy. The study therefore provides powerful evidence that organizational visibility, a variable absent from most analyses of firm philanthropy and social responsiveness, plays a significant role in shaping firm behaviour.

Public visibility as a determinant of the rate of corporate charitable donations David Campbell and Richard Slack

The rates of charitable donations against profit before tax were analysed for the years 1988–2002 for two groups of UK FTSE 100 companies. Using a method based on public recognition of company name, the two groups, controlled by mean and standard deviation market value by year for size, were categorized as high and low visibility. It was hypothesized that higher visibility companies would have a higher overall rate of corporate giving, based on the presumption that charitable involvement and associated giving would be associated with the higher need to manage a range of social stakeholder claims concomitant with the higher visibility. The hypothesis was supported at a statistically significant level of confidence.

Is there a morally right price for anti-retroviral drugs in the developing world? Ross Brennan and Paul Baines

The manufacturers of anti-retroviral drugs have been accused of putting profits before lives by enforcing their patent rights in developing countries, and so allegedly preventing people with HIV/AIDS from receiving life-saving treatment. The matter came to a head in South Africa, where, in 2001, 39 drug companies took abortive legal action to try to prevent the government from introducing legislation that allegedly undermined the WTO agreement on intellectual property rights. In 2003, the South African Competition Commission ruled that there had been 'excessive pricing' of patented anti-retroviral drugs and an agreement was struck to license several low-cost local manufacturers of anti-retroviral products. In this paper, the question addressed is whether normative marketing ethics provides useful guidance to a drug company on how to deal with the dilemmas presented by the case of anti-retroviral drug pricing in sub-Saharan Africa. Approaches based on utilitarianism, deontological and virtue ethics are compared with a self-interested approach based on maximizing shareholder value.

Public visibility as a determinant of the rate of corporate charitable donations

David Campbell and Richard Slack*

Introduction

There is a steadily growing literature on corporate community involvement and a prominent theme within this concerns corporate philanthropy expressed through voluntary charitable donations. Little is known on the structural factors that precipitate differential rates of charitable giving (against a measure of surplus such as profit). This paper seeks to address that lacuna by capturing the rates of giving for two groups of companies of differing public visibility.

The stakeholder literature has suggested for some time that a firm's strategic positioning will affect its exposure to the many claims, legitimate and otherwise, of internal and external stakeholders (Clarkson 1995). It has been noted that behaviour assumed to be partly in response to such exposure can include reporting (Deegan & Rankin 1996, Campbell 2003), types of corporate social responsibility behaviour and, in recent years, internet disclosures (Adams & Frost 2004, Campbell & Beck 2004).

The need to 'manage' stakeholder claims, therefore, may vary with structural exposure and a small number of previous studies have attempted to proxy for this by measuring, for example, a company's proximity to end user (assuming this to be a proxy for public exposure – Clarke & Gibson-Sweet 1999, Campbell *et al.* 2006). Outside the ethics and reporting literatures, models have been proposed suggesting that public visibility may be an influence on some corporate behaviours; it is from these that this paper is motivated (Miles 1987, Erfle & McMillan 1990, Jiang & Bansal 2003).

The remainder of this paper proceeds as follows. In the next section, the literature on corporate charitable giving is briefly reviewed. This is followed by a discussion on the importance of exposure and visibility in influencing corporate behaviour. This underpins the hypothesis, which in turn, is followed by a discussion of method and sample. Findings are reported upon and finally, some conclusions are drawn.

Literature and hypothesis

Previous studies in corporate charitable giving

The literature on charitable donations can be broadly considered to comprise a subset of the more general literature on corporate social responsibility. Among those papers that have specifically explored aspects of charitable donations activity, three main research themes can be identified. These are shown in Table 1.

Exposure and visibility

Of particular interest to this study is the issue of how public visibility might be a cause of variability in corporate giving behaviour. There is evidence that previous research in this area may

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Table 1: Summary of literature on charitable giving

Type of research	Examples
Moral and economic issues raised by corporate charitable involvement	Friedman (1970) Nesteruk (1989) Shaw & Post (1993) Moore (1995) Himmelstein (1997) Campbell *et al.* (1999) Pearson (2000) Dean (2001) Porter & Kramer (2002)
Corporate issues and associations between charitable donations and company characteristics	Cowton (1987) Wang & Coffey (1992) Adams & Hardwick (1998) Edmondson & Carroll (1999) Williams & Barrett (2000) Brammer & Millington (2003) Saiia *et al.* (2003) Williams (2003) Seifert *et al.* (2003), (2004)
Empirical studies – longitudinal and cross-sectional patterns in charitable giving	Arulampalam & Stoneman (1995) Weeden (1998) Campbell *et al.* (2002) Brammer & Millington (2003)

have conflated size and visibility, perhaps assuming visibility to be a function of size. Useem (1988: 81) claimed that, 'the most important single institutional factor underlying corporate giving decisions is firm size'. More recently, Seifert *et al.* (2004: 145) suggested that 'large firms have greater visibility which would attract greater public scrutiny and a higher standard of corporate citizenship'. Jiang & Bansal (2003: 1061), similarly suggested that, 'multinationals are more visible [than domestic firms]' and 'firm size may also enhance the visibility of firm's tasks'. The assumption appears to have been made (by Useem, Seifert *et al.* and Jiang & Bansal) that size confers visibility. This was also an underlying assumption in Watts & Zimmerman's (1986) political costs hypothesis where the 'size hypothesis' was described as being capable of describing differentials in political and societal exposure. The validity of this assumption is tested in this study. It sought in part to establish whether differential visibility exists when size controls are introduced.

Other areas of business research have found some aspects of corporate behaviour to respond to the differential, specific vulnerability of a company to certain issues. Reporting studies, for example, have found several such effects. Campbell (2003), Deegan & Rankin (1996) and Wilmshurst & Frost (2000) all found environmental disclosure narrative volumes to respond to the vulnerability of reporting companies to environmental risk. Clarke & Gibson-Sweet (1999) classified companies into three groups based upon their proximity to end-users. Differences in social reporting were observed corresponding to the measure of proximity to end-user. Campbell *et al.* (2006) found that voluntary narrative concerning community activities was positively associated with the reporting firm's public profile.

Inasmuch as both reporting and philanthropy can be considered to be part of a firm's broader stakeholder and reputation management effort, this study attempts to explore whether the cross-sectional effects found in reporting studies are also in evidence in corporate philanthropy. In the case of philanthropy, corporate behaviour may, it could be hypothesised, respond to the intensity of stakeholder claims associated with public visibility. Insofar that philanthropy can be assumed to be concerned in part with stakeholder management and be associated with company strategy (Saiia 2001, Saiia *et al.* 2003) those companies most likely to benefit from the management of stakeholder claims in this way would be expected to make the most use of philanthropy for such purposes. This is based upon two assumptions.

1. Higher visibility companies will, because of their visibility, have a greater and perhaps more intense range of 'societal' stakeholder concerns to manage than lower visibility companies.
2. Charitable giving is one way in which this general range of stakeholder 'societal' concerns can, in part, be managed. The giving and reporting of charitable largesse is capable of enhancing corporate reputation among this group of stakeholders.

Public visibility is, however, a problematic issue for empirical researchers. Issues raised include defining visibility and problems with its measurement. Miles (1987: 2) developed the concept of 'business exposure', to indicate the extent to which a firm has 'exposure to its social environment'. The main determinant of business exposure, Miles argued, is product mix and the presence of consumer (i.e. final user in a supply chain) demand. It was concluded that, 'in general, consumer-product companies tend to be more exposed to the corporate social environment (Miles 1987: 3). As the level of business exposure increases, there is increased pressure on companies to manage this exposure, and one way of doing so is through the management of external relations: 'The greater the degree of a corporation's exposure, the greater will be the need for executive attention and organisational resources in the area of corporate external affairs' (Miles 1987: 275).

Erfle & McMillan (1990) found public visibility to be an influence upon oil price-rise decisions. In that (for oil companies) price rises can be a source of negative public perception, Erfle & McMillan tested for – and found – that more 'visible firms will moderate price increases in visible market segments' (Erfle & McMillan 1990: 128). They concluded that 'visible firms [adopted] differential pricing to avoid consumer or market share loss' (p. 133). Jiang & Bansal (2003) found that 'task visibility' was important – the visibility of the activities conducted by an organisation. In the case of the Jiang & Bansal study, environmental issues were considered and, accordingly, activities such as tree felling conferred visibility.

The belief that philanthropy may be associated with visibility is untested in the literature, notwithstanding a *prima facie* case existing for such an association. This paper seeks to redress this deficit.

The hypothesis, rendered directionally, is as follows:

The rate of charitable donations against pre-tax profit will be positively associated with the giving firm's public visibility.[1]

Sample and method

Sample

In order to address the hypothesis it was necessary to generate a sample capable of being sorted according to public visibility that would also be of sufficient size to generate statistically significant findings. This was arrived at in several distinct stages.

It was necessary to control, as far as possible, for all variables other than visibility. In particular, it was deemed necessary to control for size effects (Trotman & Bradley 1981, Cowen *et al*. 1987, Belkaoui & Karpik 1989, Adams & Hardwick, 1998, Seifert *et al*. 2004). In order to do so, the 'large' companies of the FTSE 100 only were considered as candidates for inclusion.

The FTSE 100 listing was generated by market value at September 2003 and, using mean annual market value figures from DataStream, the FTSE 100 was generated for 1990 and 1996 (these representing points near to the beginning and middle of the longitudinal period). Any company not a member of the listings on all three dates was excluded from the study (because contiguous membership was necessary to control for size in the bifurcated groups – see later). The list of those companies that were members on all three dates was scrutinised and any that had undergone such change (e.g. by merger or acquisition) so as to materially affect public visibility over the time period in question were also excised.[2] The longitudinal element (15 years) was introduced to increase the confidence in the findings. A shallow longitudinal element (e.g. 1 or 2 years) would not have provided a sufficiently robust sample upon which to draw conclusions.

The remaining list was then sorted according to visibility. The literature was unable to offer a great deal of precedence on how to sort companies according to visibility. Ranking by proximity to end-user was theoretically possible (Clarke & Gibson-Sweet 1999) but problems of vertical integration may have made this problematic, and this apart from issues concerning the validity of assuming that proximity to end-user is a proxy for visibility. Erfle & McMillan (1990) used Television News Index and Abstracts (TNIA) as a proxy for visibility within the oil industry – effectively a media 'hits' measure.

A more direct approach was preferred that would provide primary data on the public recognition of company names. This was done by offering the derived list of companies to 500 British[3] individuals with each person being invited to tick if they had 'heard of' that company. The 500 individuals were drawn from the student populations of two universities in the north of England and from the administrative staff (i.e. not academic staff that may have biased the recognition statistics) at one of the universities.

In order to control for the possibility that some companies currently with a high 'heard of' frequency may have previously (had the question been asked) had lower visibility – and vice versa – the sample was bifurcated into 'high-' and 'low-' visibility groups. This avoided the pitfalls of attempting to interrogate the data on a continuum of relative 'fame'.

Those companies with a recognition rate of greater than 85% of the 500 responses were classified as 'high visibility' while those with lower than 25% recognition were classified as 'low visibility'. These limits were drawn in order to provide approximately equal sample sizes for high and low visibility – the recognition distribution was not symmetrical (Table 2).

Companies in the two groups were then analysed for size (mean annual market value) at the three dates (1990, 1996 and 2003). After the excision of outliers on both sides that would have skewed the mean and standard deviation sizes as at the earlier two dates, two groups of seven companies were finally arrived at. These are shown, along with the summary size statistics, in Table 2.

Table 2: High- and low-visibility groups

	Recognition (% of those asked) at 2003	Mean annual market value in £m Year 1990	Year 1996
Low-visibility group (< 25% recognition)			
Allied Domecq*	24.7	3597	4944
Land Securities	15.9	2524	3380
Reed Elsevier	13.3	2219	6266
Pearson	16.8	1862	3837
Standard Chartered	15.0	1003	6364
Smith & Nephew	23.8	1114	2136
GKN	10.6	950	3481
Mean	17.2	1896	4344
Standard deviation		974	1578
High-visibility group (> 85% recognition)			
BAe Systems	93.8	1377	4179
Royal Bank of Scotland	96.5	1273	4215
Rolls Royce	98.2	1795	3354
Legal & General	87.6	1857	3679
Cadbury	98.2	2292	5088
Boots	97.3	2838	5819
Granada	93.0	690	6786
Mean	95.0	1732	4732
Standard deviation		705	1232

*Allied Domecq was formed by the acquisition of Domecq by Allied Lyons in 1994. An anonymous reviewer pointed out that this might have affected the public recognition of the company name. The authors accept this limitation but also point out that as it occurred early in the longitudinal period under analysis, only a few years (5) could be affected by this limitation. It is unlikely, furthermore, that such a name change would have moved Allied Lyons from the 'high-' to 'low-' visibility group and so the overall distribution of public recognition data would not be materially affected by the change. The authors thank the reviewer for bringing this limitation to their attention.

Method

The relative 'generosity' of an individual or firm is measured not in absolute cash terms but in the rate of giving against the level of surplus enjoyed (the *widow's mite* principle[4]). In recognising this, the PerCent Club[5] defines giving rate as donations against pre-tax profits. For the purposes of this study, and to avoid the risks associated with establishing the nature and value of non-cash (in kind) corporate contributions, cash donations only were used. Pre-tax profit (technically, after interest and before tax – from the profit and loss statement) is a measure of accounting surplus not directly dependent on the levels of fiscal pressure in the economy and is thus a fair measure of the trading surplus of the company in the accounting period.

In the UK it has been compulsory since 1968 (the Companies Act 1967 introduced the requirement) to disclose the cash amount given to charitable causes in the year under review. Insofar that the profit before tax (PBT) figure is also available as a compulsory reporting item, both figures could be established by a simple reading of each company's annual reports for each year of the study. The figures were entered onto a spreadsheet for calculation of the ratio and to facilitate subsequent statistical analysis.

Table 3: Companies' giving against losses

Company and year	Loss (£m)	Giving (£m)
BAe Systems (1991)	81	1.31
BAe Systems (1992)	1201	0.874
BAe Systems (1993)	237	1.349
BAe Systems (2002)	616	1.134
Legal General (2001)	149	0.72
Legal General (2002)	106	0.906
Granada (2001)	105	1.1
Granada (2002)	378	1.1
Rolls Royce (1992)	184	0.247
Rolls Royce (1996)	28	0.324
Pearson (2001)	438	0.748
Pearson (2002)	25	0.868
Reed Elsevier (1999)	26	0.04
Reed Elsevier (2001)	79	0.036
Smith & Nephew (1994)	5.5	0.544

Findings

The statistical problem of giving against losses

The database generated by the analysis of the donations against profits contained 210 observations (i.e. 14 companies over 15 years). Of these, all represented donations against 'positive' profits except 15 where a donation was made despite losses being incurred in the year in question (see Table 3).

Excluding outliers

The presence of these negative ratios frustrated the ability of the research findings to generate a simple comment on the hypothesis by means of a longitudinally stacked *t*-test of 'high' and 'low' group giving rate observations. When these 15 observations were excised as effective outliers and the remaining observations were processed as a *t*-test, the separation of mean longitudinal-stacked observations (i.e. percentage ratios) was shown to be significant at the 0.05 confidence level (one tail $p = 0.003$), see Table 4.

The difference in giving rates between high- and low-visibility companies is also statistically significant when 1-year 'lagged' data are used. The crude ratio of means (high/low) for the contemporaneous comparison is 2.1 times while the same ratio for high/low when the lagged data is used is 2.4 times. This finding may suggest that

Table 4: *t*-test of longitudinally stacked (i.e. all years) 'high' and 'low' observations

	Same year		Lag by 1 year	
	High	Low	High	Low
Mean percentage	0.387	0.179	0.43	0.18
Variance	0.506	0.024	0.596	0.022
Observations	95	100	91	94
Hypothesised mean difference	0		0	
Df	102		96	
t-statistics	2.8		3	
$P\ (T \leqslant t)$ one-tail	0.003		0.002	
t critical one-tail	1.65		1.66	

Note: Figures are for same year (year *n* donations/year *n* PBT) and lag by 1 year (year *n* donations/year $n-1$ PBT). Research in other areas of accounting and social responsibility research have suggested that discretionary expenditure in 1 year might be influenced by the profits earned in the previous year (Preston & O'Bannon 1997, Moore 2001, Moore & Robson 2002). Dividends, for example, are believed to be strongly influenced by the previously earned net surplus. In order to test for this effect, additional analysis was made of the data involving the calculation of the ratio between the charitable donations in year *n* by the PBT in year $n-1$. Negative figures are excluded in both high and low groups, i.e. when loss is made.

Table 5: Totalled giving rates

	Ratio (high)	Ratio (low)
1988	0.13	0.12
1989	0.2	0.15
1990	0.3	0.15
1991	0.43	0.18
1992	0.37	0.15
1993	0.28	0.15
1994	0.25	0.12
1995	0.2	0.13
1996	0.14	0.1
1997	0.2	0.12
1998	0.21	0.09
1999	0.2	0.16
2000	0.25	0.13
2001	0.36	0.13
2002	0.31	0.16
Mean	0.26	0.136

Note: Giving rates are calculated as the percentage of total donations against totalled profits for the high and low groups in each year. *P*-value of 'high' and 'low' separation is significant to three decimal places (4.3E – 05).

Figure 1: Summed giving rates for all companies in each group by year (i.e. reducing individual company effects on total).

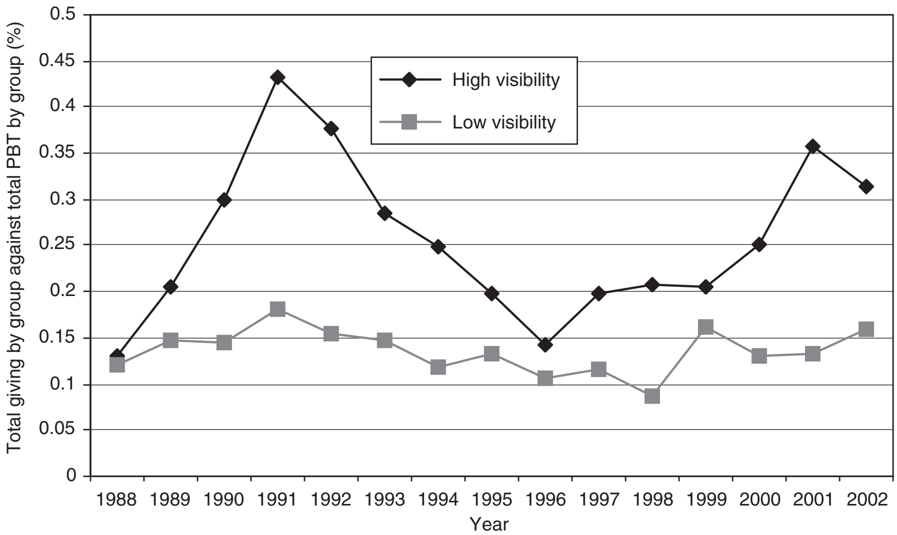

Table 6: Mean-amended figures for high- and low- visibility groups

	High	Low	Mean high/mean low (%)	Significance of separation (Mann–Whitney)
1988	0.0002035	0.000194	104.9	0.097
1989	0.0003311	0.0002397	138.1	0.6
1990	0.00051	0.0002424	210.4	0.05
1991	0.0005539	0.0002711	204.3	0.12
1992	0.125	0.0002746	45519	0.38
1993	0.0006106	0.0002872	212.6	0.2
1994	0.0004978	0.0002591	192.1	0.2
1995	0.0004895	0.0003071	159.4	0.22
1996	0.0005519	0.0002707	203.9	0.097
1997	0.0006374	0.0002828	225.4	0.097
1998	0.0007182	0.0002928	245.3	0.1
1999	0.0007923	0.0003346	236.8	0.097
2000	0.0008753	0.0003309	264.5	0.029
2001	0.00116	0.0003749	309.4	0.021
2002	0.0013319	0.0004938	269.7	0.015

Note: The table shows the ratio of high to low (second column from right) and Mann–Whitney separation statistics. The mean amended figure for the high-visibility group was 2.2 times the mean for the low-visibility group.

companies in part base their giving decisions in any given year on the size of the previous year's profits.

When company giving against profits was summed for all companies by year by group ('high' and 'low' recognition), it was possible to test for the total giving rates for the group ignoring any company effects that may skew the sample. Table 5 shows that in each year the high-recognition group gave more than the low-recognition group. Figure 1 shows this as a graph.

Range compression to account for negative outliers

In order to analyse the full data set and account for the fact that 15 observations were negative (thus expressing more 'generosity' than a giving figure against a profit) the data was manipulated to add the maximum loss (of £1201 million for BAe in 1992, plus one pound to avoid that observation itself being represented as infinity) to all denominators ('high' and 'low' groups, all years) thereby providing a data set capable of describing the scale of generosity in a meaningful manner (i.e. those that gave against losses will show as higher than those that gave substantially against profit). The purpose of the recalculation was to reconfigure all values so that those companies that gave against losses were represented by the highest figures while also showing that those that gave at the highest rates against 'positive' profits were, in turn, represented by higher numbers than those that gave more parsimoniously.[6]

A simple comparison of means of the amended figures for high and low visibility is shown in Table 6. The very high high-to-low differential in 1992 is caused by the large loss at BAe making the denominator for that company very high in that year. A cursory inspection of the other differential figures (in the penultimate column) reveals a pattern: in all years, the mean 'high-visibility' figures (amended) are at least double those amended figures for the low-visibility group. In most cases, the 'high' figure is between 200% and 300% of the 'low'. Mann–Whitney tests produced significance in the single year comparisons in four of the years analysed (1990, 2000, 2001 and 2002).

Conclusions

The hypothesis is supported at the 0.05 level. The rate of charitable giving against profit is found to respond positively to public visibility. This study has found that when size-controlled, the high-visibility companies in the sample gave to charity at a higher rate against trading surplus than the low-visibility companies over the period 1988–2002. This conclusion is made at high levels of statistical significance using both parametric (*t*-test) and nonparametric (Mann–Whitney) statistical methods. The differential does not appear to be related to time period nor is the overall difference driven by a particular part of the longitudinal period.

The study is therefore able to suggest that it is likely that companies use charitable donations as one means of responding to their public visibility. Insofar as visible companies may experience stakeholder claims not experienced by less visible companies, engagement with charitable causes and making appropriate supporting cash contributions may be a part of such claim management.

It is also worth noting that the primary visibility data in this study, controlled for size by bifurcation, allows a challenge to the view that visibility is conferred by size alone. All of the companies in the sample were members of the FTSE 100 index as at September 2003 (thereby being 'large' companies by most relative definitions) but whereas some company names were recognised by almost all participants in the survey, some – of comparable market value – were recognised by fewer than 10%. Factors such as the presence of a consumer brand or products bearing the company name are perhaps stronger predictors of visibility than size alone.

Limitations of this study include its inability to measure the totality of a businesses' donations to charities including non-cash contributions. Previous studies (Campbell *et al.* 2002) have estimated that cash accounts for approximately 75% of the total value of donations, however. In order to invalidate the findings of this paper, there would have to be a disproportionate reliance on non-cash donations by the low-visibility group of companies. There is no evidence for this.

A number of avenues for further research are suggested by these findings. Other 'testable' issues that may respond to visibility could be examined. Insofar as charitable donations are one mechanism with which some stakeholder claims might be managed, other such stakeholder-managing activities could also be explored. These might include community activities, political engagement and similar activities.

Acknowledgements

Thanks to Chris Cowton for helpful feedback on an earlier version of this paper, to Mike Cox for helping with the statistics, and to the anonymous referees.

Appendix A

Table A1: Summary statistics for all companies

	BAe	Cadbury	Leg Gen	Boots	RBS	Granada	Rolls	Std Chart	Pearson	Reed	Land Sec	Smith & Nephew	GKN	Allied Dom
Mean	0.41	0.17	0.46	0.47	0.76	0.21	0.21	0.08	0.29	0.15	0.1	0.36	0.15	0.14
Standard error	0.13	0.02	0.23	0.089	0.38	0.053	0.04	0.02	0.04	0.07	0.03	0.02	0.025	0.025
Median	0.27	0.16	0.17	0.36	0.27	0.14	0.18	0.06	0.27	0.1	0.05	0.34	0.1	0.12
Mode	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A
Standard deviation	0.43	0.06	0.84	0.36	1.48	0.19	0.15	0.07	0.13	0.24	0.1	0.1	0.1	0.1
Sample variance	0.18	0.004	0.71	0.13	2.19	0.036	0.023	0.004	0.02	0.06	0.01	0.01	0.01	0.01
Kurtosis	6.9	1.1	11.9	10.75	12.26	3.28	3.1	6.99	2.66	11	1.5	−0.02	2.2	1.05
Skewness	2.5	0.5	3.4	3.07	3.44	1.95	1.6	2.4	1.52	3.2	1.8	1	1.7	0.97
Range	1.49	0.25	3.2	1.49	5.73	0.64	0.55	0.27	0.47	0.9	0.3	0.26	0.3	0.34
Minimum	0.11	0.06	0.023	0.22	0.17	0.06	0.05	0.03	0.16	0.005	0.04	0.26	0.06	0.01
Maximum	1.6	0.3	3.23	1.7	5.9	0.7	0.6	0.3	0.63	0.92	0.34	0.52	0.38	0.36
Sum	4.56	2.5	5.96	7.5	11.45	2.68	2.7	1.26	3.7	1.96	1.5	5.05	2.23	2.15
Count	11	15	13	15	15	13	13	15	13	13	15	14	15	15

Current (same year) ratio of charitable donations to PBT as percentage. Figures exclude negative figures (hence inconsistent n values) in all cases so these figures tend towards the indicative.

Notes

1. This study tests directionally, i.e. by hypothesising that visibility is a determinant of donations rate. It is, however, conceivable that in some situations the rate of donations may be a partial influence on public visibility. The factors that have been linked with causing visibility (Miles 1987) do not include charitable donations, however. Insofar as factors such as product mix, brands and political profile are more likely to be the strongest determinants of visibility, the unidirectionality of the hypothesis is defensible. Charitable donations in themselves would be likely to have a marginal effect at most on public visibility.
2. Whitbread, for example, repositioned itself from a brewer and pub company in the mid-1990s to concentrate more on hotels and leisure. The company name itself became less prominent as a result and this change disqualified Whitbread from inclusion in the study.
3. British nationals only were included in order to control for the possibility that overseas students may be less representative of the general British population in their recognition of the companies listed.
4. A biblical allusion drawn from Mark 12: 41–44 and Luke 21: 1–3. The generosity of a gift is measured against the wealth of the giver, not in the absolute value of the gift.
5. The Percent Club is a part of Business in the Community – a group of (mainly) corporates who aim to contribute to charitable causes at the rate of 0.5% of pre-tax profits. The calculation is, however, frustrated by difficulties in the valuation of non-cash (in-kind) contributions such as product and staff time.
6. Suppose that in a sample of three companies, all of whom gave £1 in charitable donations, Company A made a loss of £3, Company B made a profit of £2 and Company C made a profit of £3. The order of generosity in this sample is therefore $A > B > C$ although only B and C reported giving against profits (A made a loss). Let us now add the value of Company A's loss (£3) plus £1 to avoid Company A's amended figure being infinity (for no mathematical reason other than a value of infinity makes statistical analysis problematic), to all denominators. Although the ratio of giving between one giver and another is now different (by compression), the order is preserved thus allowing comparative analysis to be undertaken. A becomes: £1/ – £3+£4 = £1/£1 = 1. B becomes: £1/£2+£4 = £1/£6 = 0.167. C becomes: £1/£3+£4 = £1/£7 = 0.142.

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The mainstreaming of Fair Trade: a macromarketing perspective

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Following a brief review of the development and underlying purposes of the Fair Trade movement, the paper introduces perhaps the key issue for the UK Fair Trade movement currently: the mainstreaming of Fair Trade food products. The macromarketing literature, with its focus on sustainable consumption, ecocentrism and a consequent need to change the dominant social paradigm, is used as a framework for analysing the findings of an empirical study of this mainstreaming process involving interviews with and case study material from both Fair Trade organisations and the major supermarkets which have engaged with Fair Trade. The key question that the paper addresses is whether Fair Trade, particularly as it enters mainstream markets, provides an exemplar, from within the existing dominant social paradigm, of the kinds of actions that the macromarketing literature suggests are necessary to enable sustainable consumption. Implications for both the Fair Trade movement and for macromarketing are drawn out.

KEYWORDS: Fair Trade; mainstreaming; macromarketing; sustainable consumption; ecocentrism; dominant social paradigm

INTRODUCTION

The worldwide Fair Trade movement has a history dating back at least 40 years and for much of that time it has been engaged in a gradual development in the organisations that form the movement, the range of products that it provides and hence the range of producer organisations that engage with it (see Moore, 2004, pp. 74–76). In recent years, however, the movement in the UK (which forms the focus for this paper) has seen a much more dramatic rate of development as a result of the ‘mainstreaming’ of Fair Trade food products through conventional retail outlets, particularly the supermarket ‘multiples’. With this development has come a significant change both in product quality and in marketing, with several Fair Trade brands (Cafédirect coffee and

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tea, Divine chocolate, Clipper coffee and tea, and Percol coffee, to name the most obvious) now taking their place alongside more established brands on the supermarket shelves.

With this process of mainstreaming have come related concerns that Fair Trade may have 'sold out' to the multiples, that its message may have become diluted, that it may even have 'lost its soul'. At such a critical time in its development, some reflection on what Fair Trade has become and what its future options may be, is clearly important. To aid in such reflection the macromarketing literature provides a helpful framework, while at the same time Fair Trade provides the macromarketing literature with an exceptional case study of the way in which its conceptualisations may be turned into 'programs of action' (Dolan, 2002, p. 175).

This paper, then, proceeds as follows. It begins with a short review of the Fair Trade movement, discussing its development and also its underpinning definition and purpose. It then explores the mainstreaming of Fair Trade food products to provide a basis from which the current position can be critically reviewed. A discussion of the macromarketing literature provides a backdrop against which the findings of an empirical study are described. The empirical study involved interviews with and case study material from key Fair Trade organisations and those supermarkets which have engaged seriously with Fair Trade. The paper concludes with some reflections both on the import of the macromarketing literature for the future of the Fair Trade movement and on potential developments for macromarketing as a result of this exposure to the Fair Trade movement.

THE FAIR TRADE MOVEMENT: HISTORY, DEFINITION AND RECENT DEVELOPMENTS

There have been various assessments of the Fair Trade movement (Adams, 1989; Barratt-Brown, 1993), but a more recent discussion of the development, parameters and issues facing Fair Trade is contained in Moore (2004). Starting from isolated examples of northern organisations beginning to trade with southern producers, Fair Trade developed into a small but international 'movement' in the 1960s and 1970s. Its origins were in craft goods imported directly from these southern producers and sold through 'alternative'[1] channels to a limited market of concerned northern consumers. However, food products were developed in the 1980s starting with coffee, which was marketed originally as 'Campaign' coffee in the UK—a clear signal of the radical side of the movement. As the movement gathered momentum a number of umbrella bodies were formed. IFAT (originally the International Federation for Alternative Trade but known now as the International Fair Trade Association) was established in 1989 as a worldwide membership organisation bringing together both producers and buyers. While still growing, it currently consists of over 270 Fair Trade organisations in 60 countries with approximately 65% of members based in the South (IFAT, 2005). In the UK, the Fairtrade Foundation was formed in 1994 and then became a member of the Fairtrade Labelling Organisations International (FLO) when it was established in 1997. These two organisations have been particularly significant in the growth of Fair Trade food products with FLO providing the worldwide standard setting and certification process that allows the Fairtrade Mark (a labelling device that guarantees that FLO standards have been met—see further below) to be applied to particular products,[2] while the Fairtrade Foundation, in common with other similar national organisations, provides the 'local' marketing arm—see Moore (2004, pp. 75–76) for further details.

The accepted definition of Fair Trade, drawn together by various members of the movement, is as follows:

> Fair Trade is a trading partnership, based on dialogue, transparency and respect, that seeks greater equity in international trade. It contributes to sustainable development by offering better trading conditions to, and securing the rights of, marginalized producers and workers—especially in the South. Fair trade organisations (backed by consumers) are engaged actively in supporting producers, awareness raising and in campaigning for changes in the rules and practice of conventional international trade. (FINE, 2001[3])

This definition has, in essence, two basic components. The first is to provide a working model of international trade that makes a difference to the producers and consumers that engage in it and to do so in such a way that social objectives—better trading conditions, the securing of rights and the development of consumer consciousness in the North—are met. The second and more radical component of Fair Trade is to challenge orthodoxy in business practice: to be a 'tool for modifying the dominant economic model' (Renard, 2003, p. 91) and encourage it towards more social ends.

As indicated above, of particular interest at present is the mainstreaming of Fair Trade. As food products have become an increasingly important part of the Fair Trade offering, presently representing around two-thirds of worldwide Fair Trade retail sales (see Moore, 2004, pp. 74–75), there has been a concerted move into mainstream retailing, with supermarkets representing the primary channel through which such goods are now sold. With this move has come the challenge to the Fair Trade movement of how to maintain the purity of the Fair Trade concept, while gaining the benefits of the increased volumes that access to the mainstream provides to southern producers. Various commentators have described this process as the 'subversion', 'dilution', 'redefinition' or 'reabsorption' of the concept (see Moore, 2004, p. 83 and further below). However, an alternative perspective is that Fair Trade cannot only more fully achieve its mission of supporting marginalised producers and workers by enabling their access to such channels and to the volumes associated with them, but that this is also the best way of achieving the second part of the mission. By working closely with these conventional players in international trade, Fair Trade organisations have the opportunity to challenge the 'dominant economic model' in a way, and with a degree of credibility, that would otherwise be unavailable.

The significant developments in volume caused by such mainstreaming, and hence the opportunity both for dilution and for influence, are certainly borne out by an inspection of the figures for the growth of Fair Trade. Figure 1 shows the worldwide growth in Fair Trade food

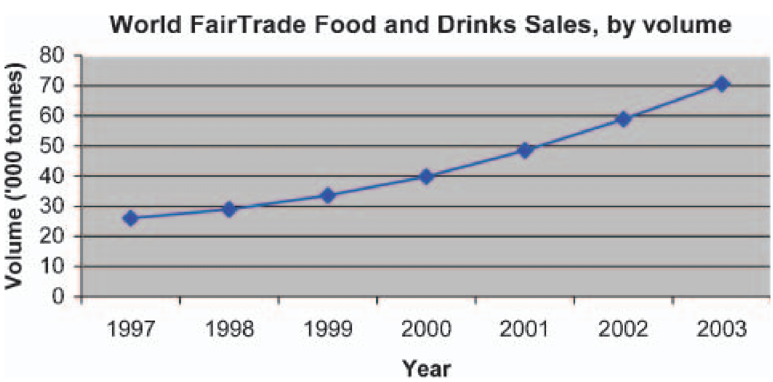

Figure 1. Source: Leatherhead Food International, 2003

Figure 2. Source: Leatherhead Food International, 2003

and drinks by volume based on FLO data. The figure for 2003 is an estimate, but the trend is clear.[4]

In terms of the main products, Figure 2 shows that bananas are the highest volume product, accounting for 62% of total volume in 2002, followed by coffee as the other significant volume product with 27% in 2002. The other products collectively make up only 11% in total. Although figures by *value* rather than *volume* were not available within this particular report, coffee is clearly the largest product by value by some way given its high price/weight ratio compared with bananas.[5]

The position in the UK is broadly similar, with sales of Fair Trade goods which carry the Fairtrade Mark having an estimated retail value of £140 million in 2004, up from £92.3 million the previous year. At the individual product level Fair Trade products have 18% of the UK roast and ground coffee market, 3% of overall coffee sales and 5% of the total UK banana market. Sales increases, by retail value, in the five years from 2000 to 2004 were: coffee 218%, tea 153%, chocolate/cocoa 358% and bananas 292% (Fairtrade Foundation, 2005a).

In terms of future projections, Leatherhead Food International acknowledged that 'the Fair Trade market is still at a very early stage of its life cycle, so it is difficult to assess its future prospects', but based on the confidence in the suppliers of Fair Trade products, the growth rate in organics as a comparator and the general interest in 'other ethical issues', it estimated that the market would 'show a 20–25% [per annum] volume and value growth over the next 4–5 years to hit a level of 150,000 tonnes, worth almost USD1billion by 2007' (Leatherhead Food International, 2003, p. 17).

These figures, of course, do not capture the whole of the Fair Trade market since, as indicated above, there are also non-food products that make up around one-third of the market size (see Moore, 2004, pp. 74–75 for a discussion of these and the various estimates of market share of non-food products). But it is clear that the main driver of growth of Fair Trade goods has been the food products and, in terms of the mainstreaming of Fair Trade through commercial channels, it is food products that have led the way. That FLO has recently introduced a standard for flowers, which Tesco and Sainsbury's retail, is an interesting non-food development that will be commented upon further below.

As far as the Fair Trade organisations are concerned, the proportion of their turnover derived from mainstream sales and hence their susceptibility to commercial and reputational risk depends, of course, on the extent of their food versus non-food sales and the range of channels through which they sell. Two examples illustrate this. Cafédirect derives a significant proportion of its turnover from selling to most major retailers, and although it also sells to the 'out-of-home' market only approximately 7% of its turnover comes from this source (Cafédirect, 2003). Traidcraft, by comparison, with a much wider product range and a greater range of distribution channels, derived only 14% of its turnover from supermarkets in 2003/04,[6] although this is expected to increase in future. Hence, the direct risks and opportunities inherent in the mainstreaming of Fair Trade vary considerably across different Fair Trade organisations. However, the focus of this paper is not on the potential impact of mainstreaming on individual organisations, but on the impact of mainstreaming on the Fair Trade movement, and the Fair Trade concept, as a whole.

THE MACROMARKETING LITERATURE AND LINKS WITH FAIR TRADE

There are three immediate links between the FINE definition of Fair Trade given above and the macromarketing literature. The first is the association made in the macromarketing literature between the 'consumption of material superfluities by the wealthy industrial nations' which is claimed to be 'at the expense of consumption of necessities in the Third World' (Kilbourne *et al.*, 1997, p. 12). While Fair Trade does not make the same causal association, there is of course a similar concern for the economic development of developing countries. The second link is the contention that Fair Trade contributes to sustainable development which resonates with the macromarketing literature's focus on sustainable consumption—this is discussed further below. The third link is in relation to notions of equity in international trade and the need to raise awareness of inequities and to campaign to change the rules and practice of conventional international trade. But while there are these points of contact, Fair Trade and the macromarketing literature also provide helpful counterpoints to each other.

Macromarketing and sustainable consumption

Within the macromarketing literature is a related set of concepts that raise questions about the direction of current trends in consumerism. At the heart of this set of concepts is that of sustainable consumption:

> Sustainable production and consumption is the use of goods and services that respond to basic needs and bring a better quality of life, while minimizing the use of natural resources, toxic materials and emissions of waste and pollutants over the life cycle, so as not to jeopardize the needs of future generations. (Oslo Symposium on Sustainable Consumption, cited in Dolan, 2002, p. 172)

By contrast with the notion of sustainable consumption are the alternative notions of 'conspicuous consumption' (McDonagh, 1998, p. 600) and 'hyper-consumption', the latter of which occurs where

> there is no logical connection between the thing consumed and the consumption act itself—it is consumption for its own sake … [there is a] total separation of the object of consumption from nature: the image is being consumed, rather than the object. … Within hyper-consumption … the sign value, or image, eclipses the commodity referent and simultaneously negates the ecological referent of the commodity as a product of nature. (Kilbourne *et al.*, 1997, p. 8)

This alternative conceptualisation of consumption links with three other parts of the macromarketing literature. First, there is the notion that historic theory construction has been anthropocentric whereas (the macromarketing literature claims) there is a need to move towards an ecocentric view in which organisations and the market place 'only exist as part of the biosphere' (McDonagh, 1998, p. 598). Second, this 'deep ecological' strand (Shrivastava, 1997, p. 170) is supported by the need to challenge the 'dominant social paradigm'—a 'society's belief structure that organises the way people perceive and interpret the functioning of the world around them' (Milbraith cited in Kilbourne *et al.*, 1997, p. 4). Kilbourne *et al.* expand on this definition as follows:

> The DSP [dominant social paradigm] in Western industrial societies informs the prevailing conception of QOL [quality of life] and provides its justification. This is manifested through the ideology of consumption, which maintains that increasing material well-being provides the basis for QOL. The quest for increasing well-being for a growing world population poses the fundamental issue of sustainability: consumption cannot increase indefinitely in a finite world. (1997, p. 5)

In order to achieve a change in the dominant social paradigm there is, third, a need to produce a 'counter-consumer' culture (Dolan, 2002, p. 176), a concept which, potentially, has resonances with notions of 'voluntary simplicity' (Rudmin and Kilbourne, 1996). While in itself a complex concept, the definition of voluntary simplicity as 'singleness of purpose, sincerity and honesty within, as well as avoidance of exterior clutter, of many possessions irrelevant to the chief purpose of life' (ibid., p. 167) provides obvious links with ecological concerns and an ecocentric view, and against conspicuous and hyper-consumption.

Macromarketing and development

It is clear from the above discussion that the macromarketing literature has obvious points of connection with limits-to-growth economics. It appears, however, that only recently has it made these connections explicit and begun to build an expanded macromarketing model that links directly with both environmental and development economics (Kilbourne, 2004). Daly (1999) provides the conceptual basis for macromarketing's ecological concerns with his 'uneconomic growth theory' in which he argues that continued growth in a 'full world' situation (where the macroeconomy reaches a level at which it 'fills' the ecosystem that surrounds and sustains it) may be uneconomic—the costs of growth may be greater than the benefits at this macro level. In such a situation, and given the unequal levels of development in different countries and parts of the world, there is, he argues, a requirement for differentiated growth in which higher growth rates in developing countries can be achieved economically only by lower or even negative growth rates in the developed world. 'It is absolutely a waste of time as well as morally backward to preach steady-state doctrines to underdeveloped countries before the overdeveloped countries have taken any measure to reduce either their own population growth or the growth of their per capita resource consumption' (Daly, 1992, p. 148).

Kilbourne (2004) also draws attention to the broader development economics debate, drawing particularly on Sen's work. Here development, both as process and outcome, is viewed in terms of substantive freedoms including, 'elementary capabilities like being able to avoid such deprivations as starvation, under-nourishment, escapable morbidity and premature mortality, as well as the freedoms that are associated with being literate and numerate, enjoying political participation and uncensored speech and so on' (Sen, 1999, p. 36). As part of the process of development a key aspect of Sen's thesis is the role of institutions in enabling such freedoms. Institutions include the market, the political system, the media and so on (ibid., p. 142) and it is not only the existence but also the complementarity of these institutions that is important (ibid., p.116). Thus, as Sen argues, 'it is very hard indeed to see how any reasonable critic could be against the market mechanism, as such' given that it is 'a basic arrangement through which people can interact with each other and undertake mutually advantageous activities' (ibid., p. 142). But this confidence in the market is tempered by the need for other institutions and public policies (themselves secured through political institutions) to provide 'conditions in which the opportunities offered by [markets] could be reasonably shared' (ibid., p. 142). It is precisely concerns over both the lack of such institutions in some cases, and institutions that promote inappropriate policies in others, that has led to criticisms of the whole globalisation 'project'—see Stiglitz (2002), for example.

While, as indicated above, the exploration of these links between macromarketing and development and ecological economics are comparatively recent, Fair Trade provides practical exemplification of some of these issues. Fair Trade's emphasis on economic development in developing countries is clearly supportive of differentiated economic growth, even though in developed countries this is related, at best, to substitution of Fair Trade for equivalent products rather than the reduction in consumption that the macromarketing literature and Daly (1992, 1999) suggest may be necessary for sustainability. Equally, in relation to substantive freedoms, Fair Trade clearly promotes labour practices including freedom of association, the payment of fair wages and the promotion of women's role in economic development—one of Sen's concerns in relation to the freedom of labour markets (Sen, 1999, pp. 115–116). Fair Trade also, and perhaps particularly, encourages institution-building through the development of local Fair Trade organisations to the point at which they can compete in the mainstream (see Hayes, 2006). Indeed, Hayes' conclusion is that, contrary to popular belief, 'the ethical consumer and Fair Trade premium are not the core of Fair Trade, but the long-term commitment of Fair Trade buyers to local Fair Trade organizations, underpinned by the preference of the ethical consumer, is a valuable, and sometimes essential contribution to the investment required by local organizations and their households to equip themselves with an efficient technology in order to compete in global markets'. In helping to achieve such institution-building in developing countries, Fair Trade also supports community development particularly through the provision of the Fair Trade premium which can be applied to community projects such as adult education facilities or the upgrade of a clean water supply (see Fairtrade Foundation, 2005b).

Changing the dominant social paradigm

Within the macromarketing literature, however, there appears to be an unresolved question over whether the significant changes that it promotes as being necessary can be achieved from within the existing dominant social paradigm, or whether such fundamental change can be brought about only through a challenge from without. Prothero and Fitchett (2000), for example, claim that 'one aim must therefore be to establish more fundamental changes to contemporary capitalism and commodity culture by employing the persuasive and communicative qualities of media and marketing practices' (p. 46) and it is subsequently evident that they claim that there are 'opportunities *within capitalism* to exploit commodity culture in such a way that contributes to a more ecologically sound way of life' (p. 47, emphasis added). They therefore promote a 'green commodity discourse' that 'could … be employed to communicate an alternative set of meanings that promotes less consumption-oriented lifestyles on the premise that quality of life would increase' (p. 50). An alternative formulation of the same 'from within' approach can be found in McDonagh (1998), who suggests that sustainable *communication* may contribute something towards a solution to problems of hyper-consumption (McDonagh, 1998 and see also McDonagh, 2002).

Kilbourne *et al.* (1997), however, seem less sure: 'If the solution to the crisis cannot be found within the DSP, a new paradigm is required in order for truly sustainable consumption to become a reality', although they then acknowledge that '[i]mplementing such a paradigm will be problematic, since this would require a transformation of the economic, political, and technological institutions that form the DSP and, consequently, a long-term sacrifice on the part of consumers and producers' (p. 7). Whether from within or from without the existing paradigm, however, macromarketing seems clear that its role is 'to inform society that the institutional emperor has no ecological clothes to wear'(!)—and this is by way of contrast with micromarketing which is 'complicit' in the 'vested interests' and 'profligate consumer society' that maintains the DSP (ibid., p. 17).

That these conceptualisations are 'fuzzy', with somewhat vague and ill-defined terms, is acknowledged within the literature (see, for example, Prothero and Fitchett, 2000, p. 51). However, this inter-related set of concepts is useful in so far as it prescribes a range of issues and provides a terminology that allows a discourse around them. The difficulty remains, however, whether such a discourse is likely to affect existing consumer patterns:

> The implications of the historical development of consumer culture is the very real difficulty, from the position of prescribing programs of action, of bringing about the cultural shift that would be required to achieve sustainable consumption. This historical development in Europe and North America entailed the emergence of a new ethic of self … the essence of self-hood is to be self-transforming, to be amorphous, to seek ever new experiences, and to continually reinvent oneself … modern consumption is about wanting to want. Its essence is insatiability. (Dolan, 2002, p. 175)

Given this 'very real difficulty', the question arises whether any existing 'programs of action' might provide at least the possibility of 'bringing about the cultural shift that would be required to achieve sustainable consumption'. As noted above, Fair Trade, with its emphasis on sustainable development, its challenge to the dominant social paradigm as it exists in relation to international trade, and with its clear links to the more recent developments in the macromarketing literature towards ecological and development economics, would seem to offer such an example. There seems to be little doubt that in its early manifestations Fair Trade did set out with the bold intention of being a tangible 'program of action'.

The key question to which this paper is addressed, however, is whether, as it has developed from niche to mainstream, its capacity to challenge has diminished as the increase in consumer awareness has been countered by a diminution in its radical effectiveness. Has Fair Trade, in effect, been co-opted? If so, then we may need to look elsewhere for better models, and Fair Trade may itself need to attempt to rediscover its radical edge. Alternatively, of course, as Fair Trade has entered the mainstream, the possibility exists that it has maintained its radical edge. If so, is Fair Trade now better able to influence both cultural norms and international trade practices and thus to go some way towards achieving the change in the dominant social paradigm that might help to realise the practice of sustainable consumption and help to achieve some, at least, of the substantive freedoms that lead to genuine development? Either way, it is clear that Fair Trade provides an exceptional case study of the kind of issues that the macromarketing literature is seeking to address. It is to that case study that we now turn.

METHOD

In order to make an assessment of the impact of mainstreaming on both the Fair Trade movement and the supermarkets, a multi-method approach was adopted. Interviews were arranged with senior individuals at three Fair Trade organisations—the Fairtrade Foundation, Traidcraft and Cafédirect. The websites of the supermarkets were also investigated to assess the level and content of their disclosure on Fair Trade issues and an analysis of their retail offerings was undertaken.

Interviews were then held with those senior individuals who were most closely involved with Fair Trade in the four key supermarkets that emerged from the research to that point—the Co-operative, Sainsbury's, Tesco and Waitrose. These interviews took place when other data had been collected and analysed and provided an opportunity to question the supermarkets about their motivation and levels of activity in relation to Fair Trade and to assess the effect Fair Trade was having on their own practices and their view of how it was impacting upon consumers. Finally, an opportunity presented itself to interview a senior individual in an additional Fair Trade organisation—the Day Chocolate Company. This proved to be a valuable addition to the research and the findings are included here within the next section.[7]

INTERVIEWS WITH THE FAIR TRADE ORGANISATIONS AND SOME REFLECTIONS

The radical edge of Fair Trade was confirmed in that, in all four interviews with Fair Trade organisations, the focus on marginalised producers in developing countries was emphasised. Fair Trade is about market access, sustainable livelihoods and empowerment for these producers and in its purest form is about remodelling the supply chain in such a way that these producers not only gain access to northern markets but are also enabled to trade successfully in them. At the same time, however, there was a strong focus on the market/consumer aspects of Fair Trade with an acknowledgement that Fair Trade is in a sense captive to the market—there is no point providing products that would not sell, or would sell only in limited quantities—and in that sense, as one interviewee put it, Fair Trade 'is kidding itself if it thinks it is changing market fundamentals'.

The mainstreaming of Fair Trade food products was seen in a positive light; it had enabled significant increases in volume for the producers and had thus enabled the extension of the concept into channels and to consumers previously untouched by it. The FLO standards and certification processes and the Fairtrade Mark were seen as key to this since they provided protection from any diminution in standards, coupled with a consumer guarantee that had become established and was trusted. The Fairtrade Mark currently has a 50% consumer recognition level (Fairtrade Foundation, 2005c), up from 39% in 2004 and 25% in 2003—a remarkable rise—and it was thought unlikely that any supermarket would launch an own-label Fair Trade product without it, although the Co-operative and Waitrose were believed to be able to do so with some credibility should they so choose.[8]

There had, however, been some limited signs of supermarkets challenging the Fairtrade Mark standards or not applying them in quite such a rigorous way as the Fair Trade organisations themselves would do. Thus the level and availability of support for producers was often less from the supermarkets, and there was a lower commitment to the long-term producer relationships that are a fundamental part of the Fair Trade relationship. Although no significant de-listings of products had taken place so far,[9] there was a recognition and acceptance that this would be a fact of life in dealing with the mainstream. This left the Fair Trade organisations with the responsibilities of providing the support to the producers themselves and also trying to maintain the long-term relationships. On the positive side, there was some evidence of a reinforcement of standards with one supermarket choosing to deal only through Cafédirect because of its direct relationships with producers which go beyond FLO standards.

The influence that Fair Trade organisations have had on the mainstream was viewed partly as direct and commercial in that the supermarkets now 'pull' Fair Trade products through the system whereas there was a requirement in the early days to 'push' products to obtain listings. Getting the supermarkets to take Fair Trade seriously (and hence to understand it to some extent) was clearly regarded as a success. The wider influence that Fair Trade seeks to achieve, however, was harder to assess and there was some feeling that any impact that had been achieved was through an involvement with the Ethical Trading Initiative (ETI) which addresses supply chain conditions in general and was therefore likely to have wider impact.[10] The question of the size of Fair Trade organisations was addressed by Day Chocolate following a comment in the supermarket interviews (see below), and the view was expressed that they needed to remain small and focused in order to maintain the credibility of Fair Trade and the Fairtrade Mark.

In relation to the 'bundle of characteristics' (Lancaster, 1966)[11] that are represented in a Fair Trade product it was accepted that these are highly complex. The focus, however, is on the inherent quality of the product coupled with strong elements of social and economic justice that are reinforced through the FLO standards which include sections on social and economic development and a separate section on labour conditions. Environmental considerations are present within the 'bundle' in that each FLO standard has a section on environmental development which includes a requirement to implement a system of 'Integrated Crop Management', and to comply with national and international legislation regarding the use of pesticides, the protection of natural waters, virgin forest and other ecosystems of high ecological value, erosion and waste management. FLO standards also encourage producers to work towards organic certification, but do not require it.

With such a complex array of characteristics it is not surprising that the Fair Trade organisations felt that getting this message across to consumers was not without difficulty. Partly this is to do with the fact that this message does not 'belong' in today's society—the Fair Trade message in relation to food products could be thought of in terms of 'help us to rig the market in favour of genuinely poor farmers' and this is both difficult to convey and contentious when northern consumers are already acutely aware of 'rigged' agricultural markets. There was some concern over the potential confusion in consumers' minds when faced with so many product labels but a feeling that the Fairtrade Mark was sufficiently clear and well-established for any confusion to be limited. Consumers were thought to fall into three categories: the informed and committed; those with a low level of understanding and interest; and those in between. Generally, consumer understanding was thought to lag activity in terms of the purchasing of Fair Trade goods (although Fair Trade organisations presumably prefer this to the alternative!).

One way of understanding the Fair Trade message that was mentioned in the interviews is in relation to reducing the 'distance' between consumers and producers. This has been discussed elsewhere in the literature. In commenting on food products, Raynolds noted that, '[i]f alternative products enter existing market circuits, their environmental and social qualities become subordinated to their price, as occurs with other commodities. Friedmann (1993) suggests that the way to counter this market discipline is to reduce the huge social distance that exists between producers and consumers' (Raynolds, 2000, p. 299). She reinforced this point by arguing that 'theoretically it is in the process of capitalist exchange that commodities become abstracted from their human and natural roots, so that price becomes their dominant characteristic' and hence contended that Fair Trade initiatives 'have begun to create new networks of exchange that escape the bonds of simple price competition' (ibid., p. 306). This concept of networks reducing social distance is discussed further in Raynolds' subsequent article in which she investigated 'how the huge social and spatial distances between Northern consumers and Southern producers might be 'shortened' within Fair Trade networks' (Raynolds, 2002, p. 404). This, of course, links directly with the macromarketing concern about hyper-consumption where the consumption act becomes abstracted from the product being consumed.

However, Wright's insightful critique of Cafédirect's advertising campaign between 1999 and 2002 suggests an alternative interpretation. She concludes that, 'a prominent reading [of this campaign] is that minority [developed or northern] world consumers can 'redeem' majority [developing or southern] world producers by perpetuating lifestyles prioritising self-gratification. Moreover, that the lives and landscapes of the majority world are consumables in their own right, alongside cash crops … My reading is that the campaign may encourage respect for difference, in the name of fairness or through invoking common human concerns, but it simultaneously invites consumption of difference confirming the 'superiority' of the minority world consumer' (Wright, 2004, p. 678). This may be a rather extreme view, but it should at least act as a warning that in reducing distance there remains the potential for conspicuous or hyper-consumption rather than a genuine 'network of exchange'.

From a strategic marketing perspective it is therefore important to transmit to consumers what Strong (1997, p. 36) described as the 'communication of the human element of sustainability'. Nicholls (2002, p. 13), in operationalising Strong's framework, suggested that brand building and information dissemination are required in order to achieve this. It seems clear, from the interviews with the Fair Trade organisations, that they perceive themselves as engaging in exactly this task of communication, information dissemination and brand building in order to get the Fair Trade message across. Cafédirect, for example, had declined to become an own-label supplier as it wanted to focus on developing its own brand. Associated with this, however, is the danger inherent within brand-building that it creates just the 'distancing' effect that Fair Trade seeks to diminish. One interviewee acknowledged the possibility that Fair Trade could become a 'lifestyle' choice which enables consumers to make a good 'political' statement while also believing that they are helping poor people. To avoid this danger, of course, requires the communication of a very clear message both to the supermarkets and to consumers. The question that arises, then, is whether they are succeeding—and in order to answer that we need to look at Fair Trade from the supermarkets' perspective.

SUPERMARKETS AND THEIR APPROACH TO FAIR TRADE

How, then, do the supermarkets approach Fair Trade? Although the growth figures and projections presented above are impressive, the first point to acknowledge is that Fair Trade, with a relatively limited product range (over 350 products according to Fairtrade Foundation (2005a and see also 2005d and further below) but across only 12 product categories)[12] represents a very small part of the products on offer in supermarket chains. Tesco, for example, stocks around 20,000 food lines. This raises the question as to why supermarkets should become involved at all in this niche market. The answer appears to be a combination of factors. Firstly, from a commercial perspective, ethical products in general and Fair Trade products in particular, are showing growth in markets that are generally mature and static—UK coffee consumption has shrunk by 2% in six years, for example (Guardian, 2004a). Hence, mainstream players cannot afford *not* to be involved.[13] Secondly, as far as certain supermarkets are concerned, Fair Trade fits with their own ethos and, as such, represents a natural extension of their product range.

Corporate disclosure of Fair Trade

An initial analysis was conducted to assess the extent and content of corporate disclosure about Fair Trade. In order to do this, corporate web-sites were inspected.[14] The websites of all supermarkets that potentially stock Fair Trade products (see Fairtrade Foundation, 2005d) were inspected and a site search was performed for 'Fairtrade' and 'fair trade' (see Table 2) and from this a summary of disclosure, in simple binary form relating to high and low disclosers, was produced (see Table 1).

The highest level of disclosure was given by the Co-operative, followed by Sainsbury's, Tesco and Waitrose, which all provided a similar level—see Table 2. The Co-operative's support of Fair Trade is encapsulated in its coffee policy: 'as a business driven by co-operative values, we are committed to play our part in taking Fairtrade out of the niche and into the mainstream'. This mainstreaming approach is supported by all the Co-operative's own-brand block chocolate and coffee being Fair Trade products.

This analysis can be compared with data extracted from the Fairtrade Foundation's list of certified retail products (Fairtrade Foundation, 2005d)[15]—see Table 3. This confirms the leadership of the four supermarkets identified above, although Booths is not far behind

Table 1. Summary of website disclosure

No/minimal Fair Trade information	Fair Trade information and policy statements
Asda	Co-operative
Booths	Sainsbury's
Budgens	Tesco
Iceland	Waitrose
Morrisons	
Safeway	
Somerfield	
Spar	

Table 2. Fair Trade web disclosures

	Co-operative	Sainsbury's	Tesco	Waitrose
Fairtrade definition	√	√	√	√
Fairtrade Mark	√	√	√	√
Fairtrade fortnight	√	√	√	√
Fairtrade policy	√	√	√	√ (linked to ETI)
Price and social premium	√	√	√	√
Fairtrade product listing	√	X	√	√
Fairtrade branded products	√	X	X	X
Case studies	√	√	√	√
Weblinks	√	√	√	√
Fairtrade and ETI	√	√	X	√

Table 3. Analysis of product, category and own brand offerings by supermarket

Supermarket	No. of products	No. of categories	No. of categories with own brand offerings
Asda	38	7	3
Booths	65	9	1
Budgens	18	5	1
Co-operative	122	16	15
Iceland	20	3	0
Morrisons	23	4	3
Safeway	29	6	1
Sainsbury's	67	14	4
Somerfield	25	6	3
Spar	9	2	0
Tesco	107	16	6
Waitrose	72	11	1

Sainsbury's and Waitrose. The Co-operative's leadership is seen particularly in the number of categories in which it has developed own brand offerings.

One of the potential issues with Fair Trade is how exactly it is defined, and whether this differs between supermarkets. Four definitions of Fair Trade were provided (see Figure 3) and might be compared with the FINE definition given above.

While using different words there is clearly a reasonable degree of conformity on the main characteristics of Fair Trade between the retailers and with the FINE definition. It is particularly

Co-operative: Fair trade seeks to guarantee a better deal for the world's most disadvantaged growers and small-scale producers. Aimed primarily at marginalized independent growers and producers in the world's poorest countries, fair trade ensures they receive payment that exceeds the market place norm and includes an additional premium to support producer development programmes.

Sainsbury's: Fairtrade is aimed at small, marginalised and disadvantaged producers. These are often small scale farmers, or independent plantations. It focuses on working with the producer, to allow capacity building and providing export opportunities to those suppliers who would not otherwise have access to them. It also involves ensuring that the terms and conditions of trading with the supplier enable them to maintain and develop good social and environmental conditions.

Tesco: Fairtrade is about fair terms of trade, local sustainability, better prices, and decent working conditions, enabling producers to improve their lot and have more control over their lives. By requiring companies to pay above market prices, Fairtrade addresses the injustices of world trade, which traditionally discriminates against the poorest, weakest producers. Fairtrade is not about charity. It is about a better deal for third world producers, because when they are paid a fair price they don't need charity.

Waitrose: When global commodity prices fall, they can have a direct impact on small-scale producers in developing countries. Many are forced into debt while others may lose their land and their homes. Consumers can help by buying Fairtrade products … The Fairtrade Foundation ensures a better deal for disadvantaged producers. [An extended description of Fairtrade standards is then provided.]

Figure 3. Supermarket definitions of Fair Trade

interesting that Tesco, the most commercial of the supermarkets, specifically mentions and elaborates on the injustices of world trade.

While all four supermarkets recognise the social premium paid to Fair Trade producers it is interesting that Sainsbury's explicitly links this to why Fair Trade products are more expensive: 'this (social) premium is reflected in the cost paid by the customer'. This raises the question as to who is the real supporter of Fair Trade—the supermarket and the customer jointly or just the customer prepared to pay more. The Co-operative, Tesco and Waitrose report the social premium, but in the absence of any price-related impact and so focused entirely on producer benefits.

Sainsbury's Fair Trade policy widens the role of Fair Trade from a corporate perspective by using Fair Trade within its overall Corporate Social Responsibility (CSR) framework as follows: 'the commitment to Fairtrade products forms a key part of Sainsbury's strategy for Socially Responsible sourcing … (and) overall commitment to Corporate Social Responsibility'. Whilst Fair Trade can facilitate a company's commitment to CSR, Sainsbury's and the Co-operative clearly distinguish Fair Trade from other forms of CSR trading, principally the difference between Ethical Trade (based on the ETI) and Fair Trade. This is important as part of identifying the Fair Trade message, so that it is not confused in an amalgam of CSR trading, combining ethical, fair and organically traded products. Waitrose, however, which has not joined the ETI on the basis that its own responsible sourcing policy is an improvement on ETI's, states that, 'While Waitrose is working towards the ultimate goal of ensuring all its own-label products are traded fairly, it is also supporting recognised schemes, such as Fairtrade …' (Corporate Social Responsibility report 2004, pp.26–27, available via their website). This would seem to have the potential to confuse rather than clarify, even if the ultimate ambition is laudable.

As part of this Fair Trade identity, all four supermarkets draw attention to their use of the Fairtrade Mark as a labelling device guaranteeing the standard. For example, Tesco states: 'The Fairtrade Mark is an independent consumer label which guarantees a better deal for third world workers and producers. The Mark is awarded by the Fairtrade Foundation'. This gives Fair Trade products an identity (aside from any associated branding such as Cafédirect, Clipper or Percol) with which consumers can associate. However, when a market-led labelling approach is adopted it may give rise to problems. The example of Fair Trade roses, which has become something of a *cause celebre* within the Fair Trade movement, is a case in point.

The case of Fair Trade roses

There has been concern within the Fair Trade movement (although it is difficult to find any hard evidence), over the introduction by Tesco of Fair Trade flowers in general and roses in particular.[16] The concern seems to focus first on the development of a FLO standard for flowers ahead of other products that were, apparently, before them in the queue for standard development. The implication seems to be that Tesco used its commercial influence to jump the queue. Second, there seems to be some concern at the Kenyan source for these flowers which apparently uses a company where worker exploitation has previously been identified and involves plantation-style farming. This may be somewhat at odds with the common conception of Fair Trade involving individual producer households or artisans, although FLO does provide standards for hired labour to cover such production. Discussion in the magazine *Ethical Consumer* (2004a, p. 38 and 2004b, p. 4) on this point was inconclusive but suggests that 'although [labour] conditions have improved in response to international campaigning, they may well not fit many people's ideas of what a Fairtrade product is'. In other words, there is concern that the FLO standards may not have been applied as rigorously as they should be in awarding the Fairtrade Mark. Third, there is concern that the pricing of these products is at the minimum Fair Trade mark-up from commercial prices. Fourth, the packaging for this product has very limited information about the sourcing of the product and, by incorporating the largely black and white of the Fairtrade Mark into mainly black and white packaging, suggests the possibility of an appropriation of the Fairtrade Mark. Figure 4 demonstrates this effect and also allows a comparison with the Tesco 'easy peeler' citrus Fair Trade product where the packaging is similar but there is explicit reference to FLO standards. The danger here, of course, is that such an approach, if true and extended more generally to other products, could have a deleterious effect on other supermarkets' perception of Fair Trade and the Fairtrade Mark, as well as affecting consumer perceptions. It is precisely these kinds of concern that have led to the charges of 'subversion', 'dilution', 'redefinition' or 'reabsorption' mentioned above.

The Fairtrade Foundation, in answer to these criticisms (Fairtrade Foundation, 2005b), responded that, far from jumping the queue, standards for Fair Trade flowers had been in development since 1999 and flowers had already been on sale in Switzerland since 2001—prior to the Tesco launch. In correspondence with one of the authors,[17] it acknowledged that one of the certified farms in Kenya had a previous history of failing to respect workers' rights, but stated that it was widely accepted that there have been major improvements in the past two to three years—precisely what Fair Trade is for in improving the position of marginalised and disadvantaged producers including those on large plantations. The packaging complies with all the rules for the use of the Fairtrade Mark and aligns it with Tesco's 'Finest' range—thereby not marginalising Fair Trade within Tesco and supporting the notion that Fair Trade is about quality. The Fairtrade Foundation, therefore, saw Tesco's packaging approach as demonstrating their commitment to making the Fair Trade range work. In conclusion, the Fairtrade Foundation's published commentary (2005b) states: 'Supporters of Fairtrade can be assured that flowers operate to the same level of standards and certification as all other products that carry the Fairtrade Mark'.

Tesco's response to the criticisms rests similarly on the application of the Fairtrade Mark: if the Mark is granted, the product is genuinely Fair Trade. However, Tesco also felt that the development of the FLO standard for flowers, despite the 18 months it had taken, had been 'the most important thing Tesco could have done for Fair Trade' because not only did it introduce a new product category but did so on the basis of consumer demand and so introduced FLO to a market-led (as opposed to its traditional product-led) approach. Within this particular case lies, perhaps, the essence of the dilemma facing Fair Trade.

INTERVIEWS WITH THE SUPERMARKETS

As indicated above, interviews were held with those senior individuals who were most closely involved with Fair Trade in the four key supermarkets—the Co-operative, Sainsbury's, Tesco and Waitrose. In relation to their various motivations for engaging with Fair Trade these were much as expected. The Co-operative cited the link with their own principles, the fact that many producer organisations are themselves co-operatives and backed this by acknowledging concerns about the negative effects of globalisation and poverty reduction. These motivations were reinforced both by the sub-committee of the Board that advises on the implementation of co-operative principles and by the Co-operative's members. Waitrose similarly cited their own partnership structure and corporate ethos so that Fair Trade 'fits' both in terms of values and commercially. Sainsbury's also cited an alignment of Fair Trade with their own values, but then added that Fair Trade fitted with a differentiation strategy and that Fair Trade products must

Figure 4. Tesco packaging for Fair Trade roses compared with easy peeler citrus

demonstrate that they are worthy of shelf space. While this would also be true for the other supermarkets, the slightly more commercial stance is clear. Tesco, perhaps not surprisingly, responded with the most commercial approach. Their motivations for engaging with Fair Trade were threefold: customer interest; a commercial opportunity in the commodity markets that the Fair Trade product range supplies; and demonstration of social responsibility. It was claimed that Tesco's engagement was not a reflection solely of responding to consumer demand, although there was obvious satisfaction in the fact that Fair Trade now 'over-indexes' (i.e. has a greater market share of Fair Trade goods at 33.4% than Tesco's average market share of 28.8%)[18]. The fact that around one-third of supermarket-related Fair Trade goods is channelled through one supermarket may give pause for thought in relation to market power.

In response to questions concerning the influence of Fair Trade on their own sourcing practices both the Co-operative and Waitrose acknowledged such impact and the Co-operative felt that Fair Trade had more generally affected the sourcing policies of supermarkets. Sainsbury's response focused more on the effect of the ETI than on Fair Trade's influence, with Fair Trade being seen as having had more impact on the marketing side, in getting the message across to consumers, than on the sourcing side. Tesco was similarly content to refer to its long-standing support for ETI and to state its contentment with its own sourcing practices and would not be drawn on whether Fair Trade had influenced the mainstream in relation to its trading practices.

Whether Fair Trade had been affected by its association with the mainstream was not easy for the supermarkets to answer. Certainly all the supermarkets confirmed their commitment to the Fairtrade Mark, despite in some cases considerable frustrations such as product development bottlenecks driven by producer need. Sainsbury's thought that the assurance it provided was one of the best at present. There was some concern that the Fair Trade organisations had displayed some naivety in their approach to the mainstream and that this would need to be monitored closely in order to maintain the robustness and credibility of the Mark. But generally there was an acknowledgment that Fair Trade's standards had been accepted by the supermarkets and thus the Fair Trade concept had not been directly affected by its involvement with the mainstream. The Fairtrade Mark would continue to be used although exceptions to this might occur. The Co-operative, for example, might seek to introduce further new product ranges for which there were currently no FLO standards available, as it had done with fairly traded wine in association with Traidcraft until the FLO standard had become available. Tesco's view was that it would continue to work with the Fairtrade Mark.

An interesting divergence of views emerged, however, in relation to the future direction of Fair Trade. Unsurprisingly all supermarkets were positive about the mainstreaming of Fair Trade. Tesco felt that, with its market share and demographic profile, it has the ability to turn Fair Trade from a 'bourgeois' concern into one that appealed across the full range of consumers and clearly this would lead to increased volume. This would move the Fair Trade consumer profile away from one based on price and exclusivity towards a broader but more price-conscious consumer profile. Waitrose, however, took the opposite view. Fair Trade had a clear niche and should continue to concentrate on disadvantaged producers in the developing world rather than on the demands of consumers in developed countries. The Fair Trade movement needed to be of sufficient size to be able to influence the mainstream, but it could have that influence without needing to continue to grow. There could be a danger in 'following the volume', partly in relation to ensuring supply chains, but also in the possible dilution of the concept. This was particularly related to Fair Trade becoming a commodity, whereas Waitrose argued that it needed to retain its ability to provide differentiated products. While the Co-operative did not express the same concerns about continued growth of Fair Trade, and confirmed its own commitment to continue to extend its product range particularly through composite products that use Fair Trade ingredients, it did confirm that Fair Trade should be 'about the primary producer and the product' and that there was a danger of 'selling out to the carrot of volume'.

In relation to the bundle of characteristics that customers are purchasing when they buy a Fair Trade product, there was a general consensus among the supermarkets. Given that, traditionally, Fair Trade customers could be classified as from the AB socio-demographic groups,[19] or from the 'liberal middle-class' with 'slightly higher values', there was general agreement that they were seeking to purchase better than average product quality with perhaps some understanding that smaller production runs and sourcing from the developed world justified the premium price. Beyond that, however, customers were perceived as buying a rather vague combination of characteristics: 'something that makes a difference'; 'a salve to conscience'; 'a belief that they are saving the world'; 'ease of conscience'; 'doing good for others'; 'better for someone down the line' were some of the phrases that were used. Asked, for example, whether they thought customers knew what the social premium associated with Fair Trade products was used for, Sainsbury's thought that they did not. In general, this set of responses seems to suggest that Fair Trade has not got its message across sufficiently and, despite the level of recognition of the Fairtrade Mark, the level of consumer understanding is thought to be limited.

Asked whether Fair Trade's environmental credentials were adequate, the majority view (one supermarket did not comment) was that they were not. It was recognised that Fair Trade had prioritised social justice issues, but there was a feeling that this was now becoming insufficient and that more priority had to be given to strengthening the environmental aspects of Fair Trade—although there was some recognition that this was already occurring. Links with the organic movement were seen as important with Sainsbury's suggesting that an integrated Fair Trade/organic label would be both feasible and desirable so long as it did not undermine the credibility of the product.

In relation to notions of sustainable consumption, three of the four supermarkets (the fourth did not comment) agreed that Fair Trade does not 'touch' this agenda: 'it is not about not eating chocolate, but about eating fairly traded chocolate when you do'—the substitution effect noted above. One view was that the further Fair Trade went into the mainstream the less impact it would have on culture. The only part of the consumption agenda that is an issue for Fair Trade is the 'healthy eating' aspect, and this tends to be problematic given that tea, coffee, chocolate, sugar and wine are some of the key products. However, there was an acknowledgement that Fair Trade is tackling this with, for example, lower sugar content in products such as muesli.

AN ASSESSMENT OF THE SUPERMARKETS' ENGAGEMENT WITH FAIR TRADE

It seems clear from the above description of the supermarkets' disclosure with regard to Fair Trade and the information obtained from the interviews that, for four supermarkets at least, their engagement with Fair Trade is a serious one. It is clear that the Co-operative leads the way in terms of their commitment to the concept of Fair Trade, their website disclosure, the number of products stocked and, in particular, their own-brand range. In terms of ideological commitment, Waitrose is clearly second even though this is not represented in the breadth of their product range. Sainsbury's approach was awaiting confirmation within the overall review of the business that was being conducted, but it may be that Fair Trade takes a more prominent place if it is believed that it would assist in whatever features of a differentiation strategy emerge. Tesco is clearly the least committed ideologically but, potentially at least, the most committed commercially. As Tesco adds further product lines to a range that already 'over-indexes' it looks set to continue to be able to claim that it is the UK's number one Fair Trade retailer by volume. Viewed from the perspective of performance over commitment, then, Tesco and the Co-operative would come out in the lead, given their success in making Fair Trade work against comparatively unhelpful customer socio-demographics.

The supermarkets' definitions of Fair Trade and the use, and promotion of, the Fairtrade Mark, suggest that, if anything, they have accepted Fair Trade at face value, and hence any concern that the concept might be in danger of serious dilution, whatever view is taken of the Fair Trade flowers case, would seem, on the evidence presented here, to be largely unwarranted.

DISCUSSION AND CONCLUSIONS

The importance to the Fair Trade movement of withstanding commercial pressures that might, in any way, dilute the concept seems clear. Holding to the FLO standards and the rigorous application of the Fairtrade Mark in such a way as to ensure the purity of the concept is clearly important not just for 'internal' purposes but also in retaining the confidence of the supermarkets and consumers alike. At the same time, however, it would appear that Fair Trade needs to convey its message more cogently so that consumers are clearer about what they are purchasing and know why they are doing so, why there is an associated premium price and what happens to the Fair Trade premium. This 'distance-reducing' communication strategy is, in itself, an onerous strategic marketing challenge through which Fair Trade must seek to simplify and convey a complex concept without over-simplifying it to the extent that consumers are faced with bland generalisations and continue to believe that they are in some vague sense 'saving the world'.

Fair Trade does not seek to promote either conspicuous or hyper-consumption and both existing and future 'distance-reducing' communication strategies, therefore, need to continue to seek to ensure that there is 'a logical connection between the thing consumed and the consumption act itself' so that it is never a case of 'the image being consumed, rather than the object' (Kilbourne, 1997, p. 8, cited above). Similarly, there must be concern over any strategic marketing approach which simply perpetuates lifestyles that prioritise self-gratification (Wright, 2004). This, however, raises an interesting tension. As Fair Trade brands seek to establish themselves in consumers' minds they could, as noted above, have the effect of becoming 'lifestyle' choices—the Fair Trade image could become, in a sense, more important than the product itself. This might lead to a further stratification of the market with a group of relatively well-informed but fickle consumers who buy the products for what the Fair Trade movement would see as the wrong reasons—for conspicuous or even hyper-consumption. This, however, underlines the difficulty for Fair Trade of needing to employ conventional 'micromarketing' techniques to promote its products, while conveying its radical message at the same time.

In relation to the macromarketing literature it would appear that Fair Trade offers something by way of progress towards sustainable consumption despite the contrary views of most of the supermarkets. Fair Trade products do, to some extent, 'respond to basic needs' and certainly in a way that 'brings a better quality of life' (Dolan, 2002, p. 172, cited above) to producers. There is an extent to which Fair Trade's underlying purpose is to alter the 'dominant social paradigm' by challenging the hegemony of the market, but it is clear that its ability to influence the mainstream, despite working closely with it over a number of years, is limited—the two supermarkets that acknowledged any influence were those which already had strong ideological motivations for supporting Fair Trade. It is also clear that there is some, but perhaps not enough, attention within Fair Trade to 'minimising the use of natural resources, toxic materials and emissions of waste and pollutants over the life cycle' (ibid., p. 172), and it would certainly be reasonable to conclude that Fair Trade has promoted an anthropocentric over an ecocentric view of the world. The supermarkets' majority view that Fair Trade needs to do more on the environmental front is surely correct, although any suggestion that this might be at the expense of its anthropocentric focus would seem to be misplaced. Fair Trade remains committed to its primary focus on the social and economic development of marginalised producers in developing countries.

Any link between Fair Trade and notions of a counter-consumer culture or of voluntary simplicity, however, would seem to be somewhat tenuous. This raises the question as to whether any approach that seeks to work alongside the mainstream, and to an extent therefore becomes dependent upon it, can ever seriously challenge the dominant social paradigm. As one commentator has put it, '… even ethical purchases is still seeing shopping as the solution to global problems' (Davidson, 2004, p. 15). Perhaps one relevant challenge to Fair Trade, levelled by Waitrose and further discussed in the interview with Day Chocolate, is for it to seek to remain small and pure, not to follow the 'carrot of volume' but, by rejecting the notion that growth is always good, live out a different approach. The reaction of marginalised producers to a strategy that would seem to limit their volume might well be hostile. Nor, at first sight, is this in line with Daly's (1992) view of the need for differentiated growth although it might make a limited contribution to Daly's (1999) larger conceptions of reduced growth in the developed world and of the requirements of 'full world' economics. It may be, however, that Fair Trade needs to engage seriously with the idea of an 'exit strategy' for producers in a way that Traidcraft (Traidcraft, 2002, p. 4), for example, has already begun. This would allow a greater number of producers to benefit from Fair Trade, with the established Fair Trade organisations acting, in effect, as incubators for fledgling local Fair Trade organisations, thereby increasing the effectiveness of Fair Trade in bringing more developing world producers into global markets, equipped with an 'efficient technology' (Hayes, forthcoming) to enable them to compete. This would not limit the growth in producers' volumes, while such exit strategies would also help to avoid dependency relationships (in both directions) between Fair Trade producer and buyer organisations.

What, then, of the impact of this case study of Fair Trade on macromarketing? We will confine ourselves here to two main points. The first follows from the discussion above and concerns the question of what kinds of 'programs for action' are envisaged that would bring about the 'cultural shift' (Dolan, 2002, p. 175, cited above) necessary to achieve sustainable consumption. If, as suggested here, Fair Trade cannot make more than limited impact in this direction, the question arises whether anything can that seeks both to co-operate with and at the same time challenge organisations that represent the dominant social paradigm. In particular, then, it raises the question whether the dominant social paradigm can ever be changed from within or whether this requires an external, and potentially revolutionary rather than evolutionary, approach. While Fair Trade provides a somewhat alternative agenda to and a critique of conventional international trade, it could well be argued that it does so from within the existing paradigm rather than outside of it. Certainly it has had some influence, but it could be suggested that this amounts only to dressing the emperor in slightly different clothes rather than exposing his ecological nakedness. The question, then, for macromarketers is whether Fair Trade offers a positive example of how they envisage their objective of a change in the dominant social paradigm being achieved, or whether we should look elsewhere.

The second point is in relation to the anthropocentric versus ecocentric world view. It has been acknowledged above that Fair Trade privileges the anthropocentric, although it probably does more towards ecological concerns than is generally acknowledged. In that sense, Fair Trade may not be a particularly good example of 'sustainable communication' or offer an example of a 'green commodity discourse' that might help to promote less consumption-oriented lifestyles. That said, the challenge that Fair Trade makes to macromarketing is whether it has privileged the ecocentric view to an unwarranted degree, and needs to take a more balanced approach. There is some evidence that macromarketing is now beginning to address this broader agenda—Kilbourne's (2004) paper and particularly the work of Sen (1999) on which it draws suggests that this is beginning to occur. We have seen how Fair Trade already grapples at a practical level with many of the substantive freedoms that Sen is concerned with in relation to development—labour practices including gender equity, institution-building of both economic and community institutions. This would require macromarketing to acknowledge that there are also serious issues of social justice that need to be grappled with. In other words, a Fair Trade critique of macromarketing suggests that it is only just beginning to theorise adequately the importance of social justice issues and the link between social and economic development and ecocentrism. If a change in the dominant social paradigm is to be achieved, it will surely need to address these issues more fully, just as much as those of its hitherto ecocentric focus.

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NOTES

[1] 'Alternative' is frequently used instead of 'Fair'. The origins of this are in the use of the term 'Alternative Trading Organisations' (ATOs) a name stemming from the early days of Fair Trade where 'fair' seemed too weak a description of the common and radical vision that forged these organisations into a movement.

[2] FLO currently sets standards for the following products: cocoa, coffee, flowers, fresh fruit, honey, juices, rice, sugar, tea, wine and sports balls, with standards for more tropical fruit and other tropical products under development. See www.fairtrade.net.

[3] FINE is an informal network that involves the Fairtrade Labelling Organizations International (**F**LO), the International Federation for Alternative Trade (**I**FAT), the Network of European Shops (**N**EWS!) and the European Fair Trade Association (**E**FTA).

[4] One of the issues in any analysis of Fair Trade is the lack of comprehensive data across the full Fair Trade product range. The Market Intelligence Section of Leatherhead Food International has produced the most recent international report, which also makes some projections, but even this analyses only Fair Trade food products.

[5] A rough estimate gives a ratio of 27, suggesting that the value of coffee sales is around 12 times that of bananas.

[6] Traidcraft internal papers.

[7] The discussion derives from these interviews which were conducted as follows, all dates being 2004: Fairtrade Foundation (19 April); Traidcraft (23 April); Cafédirect (20 May); Co-op (25 August); Waitrose (22 September); Tesco (23 September); Sainsbury's (23 September); and

Day Chocolate (14 October). In order to preserve the anonymity of the interviewees and protect the organisations, general points are not attributed.

[8] The Co-operative has, however, retailed own-label 'Fair Trade' wines without the Fairtrade Mark but with Traidcraft's name to provide reassurance and prior to the FairTrade Mark being awarded—see further below. Similarly, Tesco retails Traidcraft's tinned pineapple, which has yet to receive the Fairtrade Mark. This, however, is not an own-label product.

[9] De-listings occur when a supermarket decides that a product is no longer worth the shelf-space it occupies and would be better employed stocking another product. These are a regular feature of supermarket activity so that the lack of significant de-listings could be regarded as a positive sign of Fair Trade's ability to hold its own with other highly competitive products.

[10] The Ethical Trading Initiative was established in January 1998 with the support of the UK Government's Department for International Development (DfID) to help develop and encourage the use of widely endorsed standards, embodied in codes of conduct, monitoring and auditing methods, to improve labour conditions around the world. Membership consists of firms (including most of the Supermarkets), Non-Governmental Organisations like Christian Aid, and Trades Unions. See www.ethicaltrade.org.

[11] Lancaster's seminal paper within the economics literature introduced the idea that a good is purchased not for itself but for the bundle of characteristics that the good represents. Since different characteristics may be obtained, often in differing amounts, from competing goods, consumers are faced with choosing both which characteristics they prefer and how to make an efficient choice—how to maximise the bundle of chosen characteristics for the minimum price. Marketing theory, of course, uses much the same idea with the concept of 'benefit segmentation' capable of being traced back to a similar time as Lancaster's article (Haley, 1968). More recently, Kotler's presentation of product levels (core, basic, expected, augmented and potential—Kotler, 2000, pp. 394–396) together with the associated concept of product attributes (see, for example, Crittenden *et al.*, 2002), provide legitimacy to Lancaster's original conception.

[12] The categories accord approximately with the FLO categories (see note 2 above) and are: chocolate/cocoa; coffee; fruit juice; fresh fruit; honey; nuts and snacks, preserves and spreads; sugar; tea; wine/beer; sportsballs; and roses. In the more detailed list of separate products 22 different categories/sub-categories are recorded (Fairtrade Foundation, 2005d).

[13] Nestlé 'is believed to be planning to test a premium ''fair trade'' coffee brand carrying the Nescafé name in the UK, with a global rollout to follow' (Laurel, 2004) and Marks & Spencer's 198 Café Revives have switched all coffee to be Fairtrade Mark certified (Fairtrade Foundation, 2004). Kraft is also apparently considering launching an ethically aware brand, likely to be called 'Kenco Sustainable Development', but based on a Rainforest Alliance certification rather than Fair Trade, and with a considerably lower price being paid for green coffee beans (Guardian, 2004a, 2004b).

[14] The websites are: www.asda.co.uk; www.booths-supermarkets.co.uk; www.budgens.com; www.co-op.co.uk; www.iceland.co.uk; www.morereasons.com; www.safeway.co.uk; www.sainsburys.co.uk; www.somerfield.co.uk; www.spar.co.uk; www.tesco.com; www.waitrose.com. They were accessed between 8 March and 28 August 2004.

[15] The original data have been updated here to the latest version and contain 22 categories (see note 12 above). Note that all supermarkets with the exception of Iceland and Spar offer one or more varieties of fresh fruit. Morrisons and Safeway are still shown separately despite the takeover.

[16] Sainsbury's followed Tesco in retailing Fair Trade flowers, but the original concern arose over Tesco's introduction of these products.

[17] E-mail correspondence 16–18 November 2004.

[18] These figures were given verbally at the interview and are not necessarily current.
[19] Bird and Hughes (1997) and Nicholls (2002) both use published consumer data to analyse the 'ethical consumer' and while AB socio-demographic groups predominated in earlier studies there is evidence of a broadening of this to other socio-demographic groups. Tesco's and the Co-operative's engagement with Fair Trade is clearly a factor here.

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The Influence of Mutual Status on Rates of Corporate Charitable Contributions

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ABSTRACT. The claims by the Building Societies Association (BSA), some mutual building societies and other observers that mutual status is associated with higher levels of charitable and community involvement than public status banks are tested using the proxy of charitable donations in cash as a proportion of profits before tax (PBT). Using a sample of 31 of the remaining 65 mutual societies and the population of U.K.-based retail banks and still-independent demutualised banks, two hypotheses were tested: first, that charitable giving as a proportion of PBT over the period 1990–2003 was higher for mutuals than banks and second, that longitudinal records of charitable donations as a proportion of PBT for former mutuals will show a lower rate after demutualisation. Neither hypothesis was convincingly supported allowing for the conclusion that any claims suggesting that mutuals are structurally more generous than public companies are not supported by empirical evidence.

KEY WORDS: banks, building societies, charitable donations, community, demutualisation, mutuality

Introduction

The wave of building society demutualisations in the U.K. in the late 1980s to late 1990s precipitated a number of discussions on the respective benefits of both mutual and public status (see for example Boxall and Gallagher, 1997; Clarke, 1998; Drake and Llewellyn, 1998; Lewin, 2002). Whilst these discussions often concentrated on claimed benefits for customers (members) or shareholders and managers, a wider dimension of the discussion addressed the social and community issues associated with mutual status. Most observers appeared to express the belief that mutual status was associated with a greater focus on, and commitment to, community and philanthropic causes. Lewin (2002, p. 314) was typical of these, noting that, "mutual societies continue to perform vital social functions, often serving on the boards of local community groups, as well as regularly making sizeable local charitable donations". This sentiment was echoed in The Economist[1] when it observed that, "mutuals are seen to serve interests of the communities where they are based".

This study tested this belief by examining one particular aspect of social performance – charitable donations – and in doing so sought to address two hypotheses. The giving rates as a proportion of profits before tax (PBT) for mutual societies and their public status (plc) banking counterparts for the years 1990–2003 were captured from annual report data to enable a comparison between the two organisational types to be made over that period. In addition, and in order to examine longitudinal effects specifically amongst demutualised building societies, 'before and after' demutualisation analyses on five individual company giving rates as a proportion of PBT were undertaken.

The study concludes that with the exception of a small number of outliers, there are no marked effects in corporate charitable donation rates as a proportion of PBT between the two types (mutual and banks). The longitudinal studies provided weak evidence both ways: some demutualisations were found to be associated with lower commitment to charitable causes whilst the converse applied in others. The belief that mutual status is associated with a higher commitment to charitable and community giving was found to be unsupported.

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The debate over benefits of demutualisation

Permanent building societies originated in the late 18th century and marked a transition from 'terminating societies', whose objective had been to finance specific property development (for an overview of these origins see Boxall and Gallagher, 1997 and Clarke, 1998). Permanent building societies faced another major structural change two centuries later with the issue of demutualisation and conversion from mutual status (owned by members) to public limited company status (owned by shareholders). The demutualisation process has been discussed in the academic literature from the perspectives of both management and members (Boxall and Gallagher, 1997; Clarke, 1998; Drake and Llewellyn, 1998; Lewin, 2002; Stephens, 2001; Tayler, 2003).

The proponents of demutualisation (conversion) have focused on three main 'driver' areas: future growth, ownership structure and accountability and the benefits to existing members and management.

With regard to future growth, proponents of demutualisation have argued that in order to expand the size and profitability of the business, societies needed access to wider capital markets and external funding. By converting to public companies these two needs were satisfied, with greater freedom allowed under the Banking Act and the ability to raise equity finance (although in partial response to this, the Building Societies Act was reformed in the 1990s to facilitate higher rates of growth of building societies – see Stephens 2001).

The suggested second driver behind demutualisation was the apparent need to change from an 'outdated' mutual ownership structure to a more profit orientated shareholder structure. The principle of 'one member one vote' in a mutual structure can be questioned on two issues. First, voting rights are not a direct function of financial commitment and second, there are issues associated with the identification of members. Following conversion, voting rights would be in proportion to shareholding, thus clearly recognising the financial stake of each shareholder (Baker and Thompson, 2000). Problems with membership identity arose as the product range of building societies grew. The boundaries of membership became blurred and account holders were variously offered society membership or not depending on the nature of the account (Clarke, 1998). The need for voting clarity and accountability could, the proponents of demutualisation argued, be addressed by conversion. As a public limited company, the converted company would need to satisfy shareholders through increased share price and dividend payments. This motive, in turn, would promote profit maximisation as a key strategic objective. This need not be the case for mutuals whose objectives, because of their ownership structure, may be more varied from serving members' benefits, to wider social objectives such as a role in the community and tackling financial exclusion.

The third main argument in favour of demutualisation concerned the immediate incentive to existing members who would benefit from a financial windfall on conversion. Such a windfall, however, could also be seen as the present value of future benefits to those members should the conversion not proceed (Clarke, 1998). To protect themselves against this financial incentive many mutuals introduced charitable assignment schemes[2] to prevent so called 'carpetbagging' (Lewin, 2002; Tayler, 2003). As well as members, current management could also receive greater financial reward from conversions, such as share option schemes (Rasmusen, 1988; Tayler, 2003).

Some of the arguments in favour of mutuality directly address the alleged benefits of conversion whilst others focus on the supposed unique advantages of the retention of mutual status. The points made to counter the suggested benefits of demutualisation include the following. First, from the Building Society Act 1986 onwards, greater money market access has been given to societies to enable them to expand. It is interesting to note that demutualised societies have hitherto been below their Building Society Act money market ceiling thus calling into doubt the validity of conversion on the grounds of capital market access (Clarke 1998; Stephens, 2001). Second, and perhaps the most used defence against conversion, mutuals are said to act in the interests of members and thus do not have to satisfy the demands of external shareholders. In short, the suggestion is that mutuals can lend and borrow at more preferential rates because of the absence of the need to maximise shareholder returns in the short-term.

Drake and Llewellyn (1998) emphasised the benefits of mutuality as an ownership structure. The financial evidence for this is described by the margin between lending rates (mortgages) compared to deposit rates. Although Boxall and Gallagher (1997) found little difference in mortgage rates offered by mutuals and non-mutuals between 1984 and 1997, they found some evidence that mutuals offered higher deposit rates. The comparative advantage of mutuals in their ability to lower their interest margin is supported by Drake and Llewellyn (1998). Against this, Tayler (2003) suggested that some mutuals adopted profit orientated strategies of building up reserves by widening margins to finance future growth. More recent empirical data from the Building Societies Association's (2000) 'The Case for Building Societies' supported (albeit from a non-independent perspective) the claim that mutuals do transfer benefits to their members through lower margins.

A final argument for mutuality, and one that has become increasingly prominent in recent years, is the belief that social objectives can be better served through mutuality (Lewin, 2002; Michie and Blay, 2004). The basis of this logic is that in addition to their (in most cases) local presence (sometimes as specific as a suburb of a city) and hence local sense of accountability, mutuals may be better placed to serve social needs than public companies as they are less profit constrained and do not have the obligation to pay annual dividends. Boxall and Gallagher (1997, p. 117) put it thus: "they [the mutuals] may be able to define altruistic objectives which win the support of their members; in that case, their behaviour would have to differ from that of competing plcs." Armitage (1991) and Tayler (2003) suggested that social benevolence might also attract customers to mutuals and so further strengthen the argument against conversion. These beliefs, that mutuality is associated with greater social performance, are considered further in the next section of the article.

Mutual status, social performance and charitable giving

The belief that mutuality is associated with a strong commitment to charitable and community involvement is a prominent component in a number of discussions the mutuals and their representative bodies have participated in.

The Building Societies Association (BSA)[3], in particular, has made a number of claims on behalf of its members. In general terms, John Goodfellow, its chairman as at 2003, is reported to have said, in addressing the All-Party Parliamentary Group for building societies and financial mutuals, that, "mutuals... have much experience, not only in community involvement, but [they] are also aware of their CSR 'footprint' on those communities."[4] An inspection of a range of other BSA and mutual-sympathetic documents could easily leave a reader with the impression that mutual status is associated with a higher level of community support than public status – not simply that mutuals are socially aware but that they are *more* philanthropic because of their mutual status. One of the frequently asked questions (FAQs) on the BSA website (see bsa.org.uk/faq) emphasised that "they [the mutuals] are community based (rather than [being] controlled by the international stock markets)." Mr. Goodfellow reported elsewhere[5] that, mutuals are "closer to their local communities... than some of the very large institutions." In saying this, he was presumably intending to leave his audience with the impression that 'very large institutions' are not as close to their communities as mutuals. This sentiment echoed an earlier speech[6] made by John Heaps in 1998 (then BSA chairman) in which he concluded, "mutuality matters because it offers (amongst other issues) links with the local community that larger organisations envy."

In May 2000, a BSA report entitled, 'The Case for Building Societies' made the claim that, (p. 10) "many societies offer significant support for hundreds of local charities, sports leagues, employment initiatives and other community activities. Provision of community-based services and support *would be threatened* by conversion to plc status where the return to the shareholder is paramount and service to the customer secondary"(emphasis added). The report did not go on to explain how such support would be threatened but the reader is again left with the impression that mutual status is associated with greater community participation and hence (presumably) benevolence. A report entitled 'The Mutuality and Social Responsibility Report' (2002, written on behalf of the BSA by The Smart Company) argued that mutuals "have a core philosophy of community support and mutual responsibility." (p. 2). Is this statement, and others like it, implying that other legal forms of incorporation (such as plcs) are less associated with such virtue?

A report by the mutual-supporting research body, Mutuo in 2004 (Michie and Blay, 2004) made the claim that, "because of the social purpose inherent in many mutuals, they tend to give greater support to local charities and other such bodies than do... [non-mutual] companies." (ibid. p. 6). Additionally, the All-Party Parliamentary Group for building societies and financial mutuals reported that, "it is also impressive that mutuals contribute more on average to charitable and other good causes than do their plc counterparts." (ibid. p. 8).

Discussions in a range of other forums appear to reinforce the impression that mutuals consider themselves to be structurally more community-minded and socially benevolent and the reason most often given for this is the absence of shareholders.

This argument has been advanced by a number of the mutuals themselves. The Newcastle Building Society, for example, made the following disclosure on its website:

> What would we lose if you were to convert?
>
> The Newcastle are [sic] very active in the communities in which we operate. We believe it is important that we interact with the public, and that they perceive us as a friendly caring organisation which values customer loyalty, gives value for money, and contributes to the current and future well-being of the community. Our support to the communities in which we work include our Newcastle Building Society Community Fund, through which we are able to support a number of grass roots voluntary projects and charities in the areas surrounding our branches. We also have an Annual Charity Challenge where our staff, and customers, raise money for a good cause. The Society also makes a sizeable contribution. *It is likely that, due to the need for profit maximisation, we would have to withdraw from these projects should the Society convert.* (website www.newcastle.co.uk examined 12th December 2003. Emphasis added at the end to show key point).

Newcastle is not alone in conveying this threatening message. Similar support for mutuality and the role of Building Societies in the community against public status and satisfying the demands of shareholders are demonstrated by the following extracts:

> The West Brom [West Bromwich Building Society] has been a mutual building society for over 150 years and is committed to staying that way. That is because, as a mutual building society, we don't have to pay dividends to outside shareholders.... *It also means that we can continue to operate in the best interests of our members and the communities we serve.* (website www.westbrom.co.ukexamined 6th January, 2004. Emphasis added.)

> Mutuality means that your Society [the Cheshire Building Society] is owned by its members rather than external shareholders whose main interest is profit. Our aim is to use our mutual status to provide the best possible products and levels of service that we can for our members. And, by giving a percentage of our annual profit to a range of local charities, we aim to help those in the community we serve. (website www.thecheshire.co.uk examined 6th January, 2004)

> A mutual building society is an organisation that is run entirely for the benefit of its members. In contrast to high street banks, a mutual building society, like The Nottingham, does not have to maximise profits to pay dividends to outside shareholders. This means that extra benefits can be passed on to customers. The record of mutual building societies, compared to banks, shows that building societies consistently offer better value products by putting 'people before profit'. *This is a sound reason for Nottingham Building Society staying a mutual society and so continue to serve the best interests of its customers and the wider community for many years to come. The Nottingham is a community-based building society committed to the region it serves.* (website www.thenottingham.com examined 6th January, 2004. Emphasis added.)

Hypotheses

Given the foregoing discussion and the belief by the BSA, sympathetic bodies and the mutuals themselves that mutual status is associated with higher social performance in general and charitable giving in particular, two hypotheses are proposed.

H1: Mutual societies historically donate to charity at a higher rate as a proportion of PBT than public banks.

H2: Demutualisation is associated with a decline in the rate of charitable giving as a proportion of PBT.

The extent to which the rate of charitable giving as a proportion of PBT can be accepted as a proxy for community involvement, philanthropy and other expressions of benevolence may be a matter of some debate. Previous studies have made this assumption (Campbell et al., 2002; Neiheisel, 1994). An organisation may express its benevolence in a number of ways including cash donations and donations in kind such as product donations, staff secondments, subsidised consultancy etc. The measurement of any of these measures could, in principle, provide an indication of benevolence without describing the totality of an organisation's charitable and community involvement. Whilst charitable donations as a cash figure would clearly be a poor proxy for benevolence as larger organisations would be expected to give more than small companies (Adams and Hardwick, 1998; Seifert et al., 2003), this study suggests that giving as a proportion of PBT is an acceptable indication of benevolent intent. This is for two reasons. First, the 'widow's mite[7] principle' suggests that it is not so much the amount given that indicates benevolence but the proportion of the giving against the wealth of the giver. Second, the rate of charitable donations as a proportion of PBT is the measure used by the U.K.-based Business in the Community (i.e. the Percent Club) to measure benevolence and is one that companies seeking to be seen as benevolent might seek to maximise.

Some benevolence indices (the Guardian's 'giving list' in particular) claim to measure corporate donations using both cash and non-cash metrics. Valuations based on 'global community investment' allow companies to misleadingly value their giving using a range of robust and not-so-robust valuation methods. U.K. GAAP does not include a protocol for the valuation of in-kind giving (e.g., staff time, surplus stock) and so companies may value at full opportunity cost if they so wish. This might include valuing excess stock distribution at full retail price, staff time including all overheads or use of company premises at full business charge out rate. In order to avoid these pitfalls and to only measure a figure reported according to a standard accounting protocol (thus guaranteeing consistency of measurement), this study captured only cash donations.

Sample and method

In order to allow like-for-like comparisons despite size differences and to enable cross sectional and longitudinal comparisons to be made (and for the reasons given in the foregoing section), the convention of measuring 'benevolence' as charitable donations in cash terms divided by reported profit before tax in the same year was employed in all cases and expressed as a percentage.

The longitudinal period 1990–2003 was chosen for several reasons. For hypothesis 2, it provided a convenient period of 7 years pre and post the modal demutualisation year of 1997 (when four of the five demutualisations considered in this article took place). For hypothesis 1 (comparing historical giving rates for mutuals and banks), it provided a dataset of 434 observations for mutual (31 mutuals societies over 14 years) and 98 for banks (7 banks over 14 years). Only those building societies that did not convert over the period were included in the data for hypothesis 1 to ensure sample consistency. The five societies that demutualised are not included in the dataset for hypothesis 1 and these are separately considered by hypothesis 2. The building societies and banks selected for the study were based on the need to have sufficient cross sectional presence to ensure the validity of any conclusions drawn.

The sample selection for H1 was organised in two stages: selection of mutuals and selection of banks. There was a substantial size distribution amongst the 65 building societies that had mutual status at the time the research was conducted (between late 2003 and early 2005). A total of 31 societies were included in the study and these were sampled so as to include all of the top 20 by asset value and then a remainder spread evenly throughout the remaining size distribution (see Butler's Building Society Guide, 2003). When aggregated, these 31 societies comprised 94.5% (2002 figures) of the total asset value of the building society 'movement' and so adequately represented an indication of total giving rates over the period of the study.

The banks were chosen so as to exclude merchant banks but to include all of the better known 'High Street' or retail banks that building societies will in part compete against for customer attention. The sample comprised seven banks (listed in London) that had been public for the duration of the study.

The sample for H2 was derived from the need to capture those companies that had demutualised during the period of the study (to enable the 'before and after' comparisons to be made). These were more-or-less self-selecting: the major demutualisations in the period were Woolwich, Northern Rock, Halifax, Alliance & Leicester (all 1997 demutualisations) and Bradford & Bingley (year 2000). All of these companies were included in the sample.

The required observations (charitable donations and PBT for each company in each year) were obtained from the annual reports of the organisations in question – donations from the mandatory disclosure of that item in the directors' report and PBT from the profit and loss statement. Donations and PBT observations were entered onto a spreadsheet to facilitate the calculation and comparison of giving rates for each company by year and in total.

Findings

Hypothesis 1: Giving rates for mutuals and public listed banks

Figure 1 (data in Table I) shows that the mean giving rate increased over the 14-year period for both mutuals and banks (outliers have been excluded for banks for years 1990–1992[8] and one observation

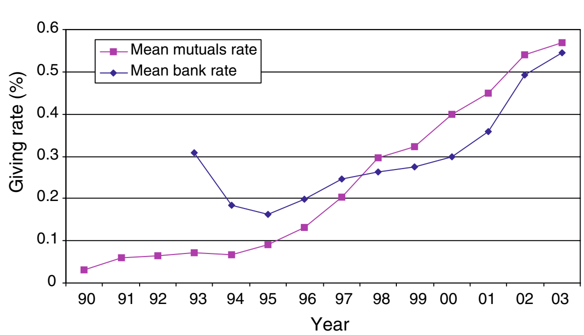

Figure 1. Mean of giving rates for mutual building societies and banks (given as a percentage of PBT) 1990–2003.

for a mutual in year 2000 to allow scale to be shown for the two series – see outlier observations in Table I). Although giving was initially lower for the mutuals, the mean rates showed convergence by the mid-1990s and remained at similar levels until the end of the period.

When, in contrast to the 'mean of giving rates' approach, the giving rate is calculated for total giving over total PBT by 'type' (i.e. for all banks and for all mutuals), the picture looks slightly different (Table II). Figure 2 shows changes in the value of donations in money units listed in Table II. The year 1996 has been scaled as 1 for both variables and all other observations have been calculated from those. It is evident from this that a switch in giving occurred amongst the mutuals in 1998 so that whereas prior to that year, year-to-year changes were comparable to the banks, after that date year-on-year changes took an upturn against the banks. It is difficult to find a reason for this but it is conceivable that the increased scrutiny arising from the public debate over the benefits of mutual status may have had an influence.

Figure 3 shows the same effect using the ratio of total giving as a proportion of total PBT for both banks and mutuals (the ratio data shown in Table II). Prior to 1997, the mean giving rate was consistently higher than the mean rate for mutuals. After 1997 (the modal year for demutualisations) the mutual rate was higher than for banks.

Hypothesis 2: before and after demutualisation

There were five major demutualisations in the period under analysis. These were as discussed below.

Northern Rock

Prior to its demutualisation in 1997, Northern Rock made no reportable charitable donations. Prior to the establishment (upon demutualisation) of the Northern Rock Foundation in 1997, all donations to charitable and community causes were channelled through the 'Promotional and Benevolent Fund' which was, by the company's own admission, a part of the company's marketing effort and therefore not exclusively benevolent in its aims. Through private correspondence with Northern Rock it was established that the company made a £650,000

TABLE I

Mean of giving rates (in percentages) for mutual societies and banks for years 1990–2003 inclusive

	90	91	92	93	94	95	96	97	98	99	00	01	02	03
Mean mutuals rate	0.03	0.06	0.076	0.07	0.07	0.09	0.13	0.2	0.3	0.32	0.58	0.45	0.54	0.57
Mean bank rate	0.34	0.9	1.7	0.31	0.18	0.16	0.2	0.25	0.26	0.27	0.3	0.36	0.49	0.55

TABLE II

Total charitable donations and PBT figures for the samples of mutuals and banks. Ratio is proportion of total donations over total PBT (i.e. not the mean of ratios by company)

		90	91	92	93	94	95	96	97	98	99	00	01	02	03
Banks	Donations (£M)	11.6	12.2	15.4	11.9	14.7	14.8	21.7	35.0	40.8	45.8	59.4	72.8	64.1	44.6
	PBT (£bn)	2.89	2.98	3.36	6.36	9.65	11.5	12.9	13.6	13.6	14.0	20.1	19.9	16.0	8.2
	Ratio as %	0.40	0.41	0.46	0.19	0.15	0.13	0.17	0.26	0.30	0.33	0.29	0.36	0.40	0.54
Mutuals	Donations (£M)	0.41	0.77	0.47	0.70	0.83	0.81	0.99	1.22	4.00	4.40	10.4	5.10	6.64	5.36
	PBT (£bn)	0.58	0.58	0.48	0.55	0.70	0.81	0.81	0.50	0.82	0.98	0.94	1.1	0.89	0.91
	Ratio as %	0.07	0.13	0.10	0.13	0.12	0.10	0.12	0.25	0.49	0.45	1.11	0.47	0.75	0.59

contribution to its Promotional and Benevolent Fund in 1996 (the year before demutualisation), which, as a proportion of its PBT of £147 million, represented a giving rate of 0.44%.

The 1997 demutualisation was accompanied by the establishment of the Northern Rock Foundation. The company announced its intention to donate, annually, 5% of PBT through the Foundation, which, although criticised at the time of being a mechanism against takeover, may also have been an attempt to clarify the motives behind the company's charitable involvement. The giving rate as a proportion of PBT of 5% has been equalled or exceeded in each year subsequent to the demutualisation. This rate represented a greater than 10-fold increase over pre-demutualisation levels.

Alliance and Leicester

Alliance and Leicester demutualised in April, 1997. This study was able to examine annual reports for

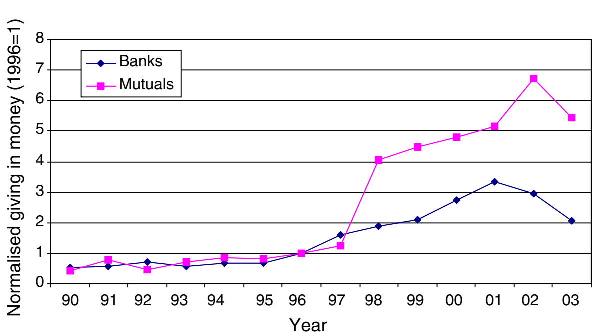

Figure 2. Giving for mutuals and banks in money units (scaled to 1996 = 1) to show relative rates of increase. Excludes one high outlier for mutuals in year 2000 to enable graph to show comparative figures.

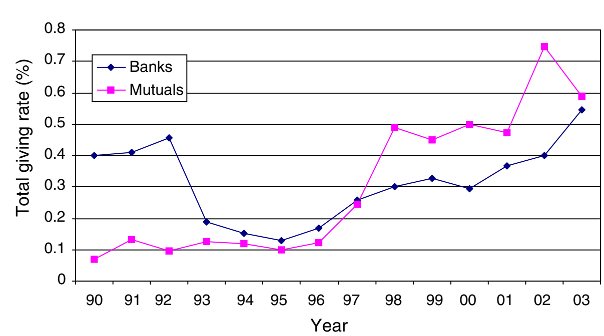

Figure 3. Totalled giving rates for the samples of mutuals and banks (i.e. the ratio data from Table II). Excludes one high outlier for mutuals in year 2000 to enable graph to show comparative figures.

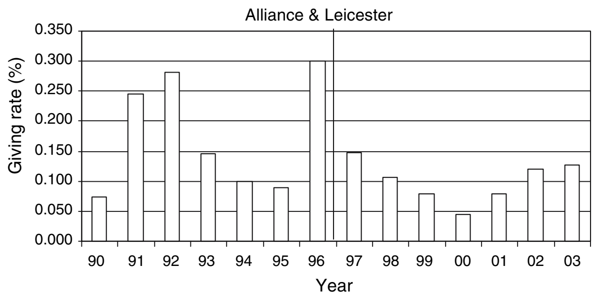

Figure 4. Alliance & Leicester – longitudinal record of giving rate as percentage. Vertical line indicates point of demutualisation. Mean giving rate before demutualisation was 0.17%, after was 0.09%. $p = 0.04$.

the years from 1990 to 2003 inclusive and thus provide a record of charitable donation rates for several years before and after demutualisation (Figure 4). The trend appears to show a slight decline in donations as a proportion of PBT after demutualisation and a statistical comparison of the 'before and after' data supports the belief that the rate of giving fell after demutualisation ($p = 0.04$).

Woolwich

Woolwich annual reports were examined for all years from 1990 to 2003 although in October 2000 it was acquired by Barclays plc. The demutualisation date was July 1997. Figure 5 shows the longitudinal record of giving rate. No obvious 'before and after' effects are apparent and this observation is borne out by calculation of means (0.121% before and 0.095% afterwards). The one outlying observation at year 2001 (representing a rate of 0.19% of PBT) was after the Barclay's acquisition and it was reported that, "from 2001, Woolwich participated in Barclay's Community Support programme which is administered by Barclays PLC. The Woolwich's share in that community support programme ... [included] ... £715,000 ... of charitable donations." (Woolwich 2001 Annual Report, p. 3). The post-demutualisation mean may have been lower had this participation not occurred. It might also be noteworthy that it was because of Woolwich's participation with a scheme initiated by a public company (Barclay's) that the erstwhile mutual achieved its highest giving rate of the longitudinal period in question – a rate substantially higher than its pre-demutualisation mean.

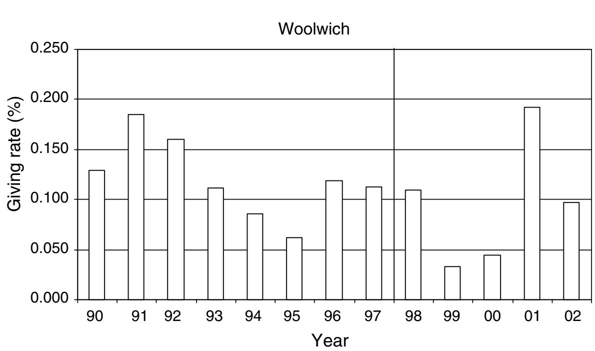

Figure 5. Woolwich – longitudinal record of giving rate. Vertical line indicates point of demutualisation.

Halifax

Halifax showed a low rate of giving until the year just prior to its demutualisation (Figure 6). Prior to 1996, its mean giving rate was 0.1%. The one-off increase in 1996 at 0.29% immediately preceded demutualisation, after which – until its integration with Bank of Scotland in 2000 – the mean rate was 0.22%.

Bradford & Bingley

The giving rate for Bradford & Bingley showed three distinct episodes (Figure 7). Prior to 1997, the rate was low (mean for 1990–1996 inclusive was 0.04%). There was a sudden switch to a much higher rate in the 3 years immediately preceding demutualisation (for the years 1997, 1998 and 1999 when

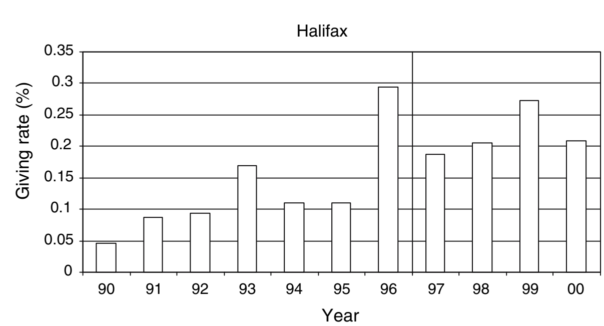

Figure 6. Halifax – longitudinal record of giving rate. Vertical line indicates point of demutualisation. Mean giving rate before demutualisation was 0.13%, after was 0.22%. $p = 0.018$.

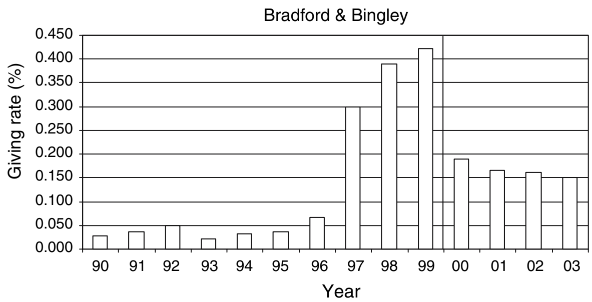

Figure 7. Bradford & Bingley – longitudinal record of giving rate. Vertical line indicates point of demutualisation.

the mean rate was 0.37%). In the third episode, for the 4 years after demutualisation, the rate reduced to a lower level of a mean of 0.17%.

Conclusions

The findings from hypothesis 1 show that there is no statistically significant evidence to support the belief that mutual societies are structurally more generous than banks when cash donations as a proportion of pre-tax profits are measured. Excepting an episode in the mid to late 1990s, when mutuals' year-on-year increase rose slightly higher than for banks, rates for both types of organisation are historically comparable.

The findings from hypothesis 2 show that there is no consistently discernible pattern in respect to giving rate after demutualisation – in some cases it rises (e.g., Northern Rock) and in others it falls (e.g., Alliance & Leicester).

The discovery of mixed findings like those from this study make the drawing of 'hard' conclusions difficult, but they do enable comment to be made on the claims made by mutual societies, and the BSA in particular, that mutual status is associated with higher charitable involvement. The belief that mutuals are more committed to their communities and express this by charitable donations at a rate higher than for demutuals and banks is difficult to support. Whilst local and regional mutuals may feel a fiduciary duty to a particular, perhaps regionally located stakeholder profile, the pressure to be community-minded might be as strong or even stronger to a demutual or a bank that is likely to experience 'moral' pressure from a more disparate stakeholder profile than the typical mutual.

Organisations in both situations clearly feel the need to make charitable donations but the internal spread and the outliers in each category make it difficult to maintain the belief that mutuals are intrinsically more 'generous' than banks.

Appendix 1

Mutual societies analysed in this study

Britannia, Cambridge, Chelsea, Chesham, Cheshire, Coventry, Cumberland, Darlington, Derbyshire, Furness, Hinkley & Rugby, Ipswich, Kent Reliance, Lambeth, Leeds & Holbeck, Leek United, Manchester, Mercantile, National Counties, Nationwide, Newcastle, Norwich & Peterborough, Nottingham, Portman, Scarborough, Skipton, Staffordshire, Stroud & Swindon, Universal, West Bromwich, Yorkshire.

Banks analysed in this study

Abbey National, Barclay's, Bank of Scotland (HBOS), HSBC, Lloyds TSB, National Westminster (Nat West), Royal Bank of Scotland (RBS).

Acknowledgements

The data collection for this study would not have been possible without access to the excellent library of the Building Societies Association in London. We would, in particular, like to thank Simon Rex of the BSA for his help in this regard. Other corporate reports used in the study were obtained from the managed archive at Northumbria University and we would like to thank Richard Pears for his adroit management of the archive and for obtaining other documents as needed. Finally, we would like to thank an associate editor and two anonymous reviewers for Journal of Business Ethics.

Notes

1 On 5th January, 1999, p. 68.

2 Members joining the Society agree to assign any future windfall gains arising from conversion to a nominated charity, thereby making no personal financial benefit.

[3] The Building Societies Association is an 'umbrella body' and represents the interests of the majority of mutual building societies.
[4] Reported on the BSA website (www.bsa.org.uk, 28th November, 2003).
[5] Speech given to the Building Societies Association's annual lunch, London, 13 November 2003.
[6] Speech given to the Building Societies Association conference, London, 3 September 1998.
[7] A biblical allusion drawn from Mark 12: 41–44 and Luke 21: 1–3. The generosity of a gift is measured against the wealth of the giver, not in the absolute value of the gift.
[8] A small number of outliers (two observations) are omitted because they would have inordinately skewed the mean for banks. The profits for Nat West and RBS suffered sudden deteriorations in 1991 and 1992 thereby dramatically increasing the giving rates in those years. The inclusion of bank means for those years would have meant the graph would not be scaled so as to show the comparison it currently does. Hence the omission.

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Publication 4

Campbell, D. and Slack, R. (2007), ‘The strategic use of corporate philanthropy: building societies and demutualisation defences’, *Business Ethics: A European Review*, 16(4), pp. 326-343.

Executive summaries

The strategic use of corporate philanthropy: building societies and demutualisation defences David Campbell and Richard Slack

This paper examines the strategic use of corporate philanthropy in the 1990s by UK building societies faced with an intensification of societal pressure to change legal form from mutual to corporate status. While the economic case for mutuality has been made elsewhere, this paper examines the observation that community relationships were thought by management to be capable of assisting in the strategic positioning of mutual societies with regard to their legal form. By increasing charitable giving to respond to the level of societal scrutiny and discussion on the issue of mutuality, this paper argues that charitable giving, as one proxy for community involvement, was used as a strategic tool to deflect calls for demutualisation, thereby preserving the existing mutual status of building societies.

Board diversity in the United Kingdom and Norway: an exploratory analysis Johanne Grosvold, Stephen Brammer and Bruce Rayton

This paper examines the evolving pattern of gender diversity of the boards of directors of leading Norwegian and British companies on a longitudinal basis. The period covered by the study covers the run up to proposed affirmative action legislation in Norway and, as such, affords an insight into corporate actions in this emerging institutional context. The findings demonstrate that, while board diversity has grown substantially in both countries in recent years, it has done so considerably more rapidly in Norway than in the United Kingdom. The analysis highlights the sectoral variation between the countries in the pattern and growth of board diversity and suggests that the vast majority of the overall growth in board diversity is the result of changing firm behaviour rather than sectoral shift in the United Kingdom or Norwegian economies. It is also shown that as diversity has increased there has been no fall in how experienced female directors are; neither is there evidence of a rise in the number of boards that female directors sit on. This suggests that the rapid growth in board diversity has been achieved without any fall in the quality of female directors.

The shadow of MacIntyre's manager in the Kingdom of Conscience constrained James A. H. S. Hine

This article addresses the issue of moral compunction among a sample of senior managers set against the background of their routine organizational participation. In considering what factors influence their moral sensibilities these managers were interviewed using an approach designed to elicit their perceptions concerning both the ethical and commercially imperative dimensions of their working lives. The qualitative data resulting from this inquiry, while tentative, indicates the primacy of the normative appeal of shareholder value, conditioned by the exigencies of engagement in corporate bureaucracies, including the maintenance of career and livelihood responsibilities. These conclusions indicate the magnitude of the obstacle that the normative business ethics project requires to overcome in order to fulfil its promise.

Two case study scenarios in banking: a commentary on *The Hutton Prize for Professional Ethics*, 2004 and 2005 David Molyneaux

The 'Hutton Prize for Professional Ethics' of The Chartered Institute of Bankers in Scotland is awarded annually to the author of an essay that addresses most convincingly the question, 'what do *you* now do?' in response to an ethically sensitive, case-study scenario. This paper makes available the Scenarios from 2004 and 2005, together with commentary thereon. Scenario 2004 stresses the importance of moral imagination and empathy. It addresses borrowing arrangements for a mother and daughter where illness has created past and continuing problems and there is the possibility that a wealthy relative will be made an unwitting guarantor. Scenario 2005 explores the boundaries inhibiting an opportunity for showing 'mercy' by one employee for another. Particular attention is paid to the difficulties that practising this ethical virtue could cause in a professional context, including tracing back to similar ambiguities discernible within foundational texts for Christian ethics.

The natural environment as a salient stakeholder: non-anthropocentrism, ecosystem stability and the financial markets Simon D. Norton

The current debate as to whether the natural environment should be accorded stakeholder status involves an assumption that it is in some way 'different' from other stakeholders, requiring favourable discriminatory treatment. Essentially it is regarded as passive, requiring regulatory agencies to represent its interests or the wider public to demand its protection on the occasion of, for example, oil spills that leave wildlife in a visibly distressed state. But the natural environment does not have 'consciousness' as do traditional classes of stakeholders such as employees, shareholders and contractors, nor does it negotiate in markets over the price at which it sells its output in the way that a trader haggles with potential buyers. This paper proposes that in the context of financial markets the natural environment possesses stakeholder status, founded upon the essentiality of ecosystem stability for their proper functioning and the structuring of instruments traded on them.

That's not what happened and it's not my fault anyway! An exploration of management attitudes towards SRI-shareholder engagement Wim Vandekerckhove, Jos Leys and Dirk Van Braeckel

This paper explores semi-formal interactions between SRI-investors that take the governance route rather than deploy a best-in-class logic or exclusionary screening. On the basis of a stakeholder typology of the investor and of the chosen topic of interaction, namely compliance with the core ILO labour conventions, the paper formulates 10 expectations about management reactions to the concerns raised by investors. These expectations cover responsiveness, acknowledgment of positions and general attitude. The expectations are then related to the factual discourse by management responding to such concerns raised by investors. Based on data obtained from the Portfolio21-correspondence, which is a joint initiative of European investors, it is found that management is very willing to discuss cases but at the same time denies the truth-value of the allegations. Here, the problem of information asymmetry comes to the fore.

Business Ethics: A European Review
Volume 16 Number 4 October 2007

Do corporate codes of ethics reflect issues of societal transformation? Western German and Slovak companies compared Ingo Winkler and Anna Remišová

Can differences in corporate codes of ethics arise from the specific situation of transformation in Slovakia in contrast to the stable context of the firms in Western Germany? This paper compares codes of ethics of large-scale enterprises in both countries in terms of ethical issues addressed. It demonstrates that codes of ethics of the Slovak companies mirror the specific transformational circumstances in the country. Compared with Western Germany the codes of these firms include multiple ethical issues, meaning that they experience a broader range of relevant ethical problems. Furthermore, their codes are internally oriented, in terms of the ethical issues raised most often; they put more emphasis on committing employees, managers and shareholders/owners to the firm. Based on the differences discovered, it is proposed that negative experiences within the past process of transformation and in part the socialist heritage are the main reasons for differences between the two samples.

Business Ethics: A European Review
Volume 16 Number 4 October 2007

The strategic use of corporate philanthropy: building societies and demutualisation defences

David Campbell and Richard Slack*

Introduction and motivation for the study

The literature on corporate philanthropy reflects a discussion among scholars on its purposes and motives. At the superficial level, it is anomalous that business organisations, whose primary *raison d'être* is profit generation, would choose to donate money to charitable causes. Campbell *et al.* (2002) analysed possible motives in terms of the altruistic, the political, the managerial utility and the strategic. Inasmuch as the probing of motives is experimentally problematic, few studies have attempted to do so.

Post & Waddock (1995) drew a helpful distinction between 'philanthropy strategy' ('the firm is orderly in the methods and procedures it uses to give money away' – Saiia *et al.* 2003: 185) and 'strategic philanthropy' ('the corporate resources that are given have meaning and impact on the firm as well as the community that receives those resources' – Saiia *et al.* 2003). Strategic philanthropy was later described by Thorne *et al.* (2003) as being the 'synergistic use of a firm's resources to achieve both organisational and social benefits' (Thorne *et al.* 2003: 360). Thus, strategic philanthropy ostensibly has a dual objective of corporate value-added and charitable benevolence. Importantly, strategic philanthropy imputes to donors motives other than altruism in their engagement with charitable involvement.

The study of corporate philanthropy as a strategic instrument is of potential policy interest for two reasons. From an agency perspective within the dominant capitalist corporate governance paradigm, the allocation of company resources for any purpose must attract a return of value to shareholders. While the incurrence of other business costs can be clearly seen to have the potential to provide such investor value, the same is less obvious for charitable contributions. From a policy perspective, an understanding of the strategic use of philanthropy would potentially underpin future philanthropy and other types of community involvement. The second reason why the study of strategic philanthropy is of policy interest is because it has the potential to assist in charities' soliciting strategies. In addition to noting an overall increase in corporate community involvement generally, a UK Charities Aid Foundation research report in 2006 found charities seeking to develop longer-term 'partnerships' with corporate givers based on mutual interests rather than resting on 'one-sided' altruism. The reason for this is obvious: relationships built on identified gain to the donating company are likely to be more enduring and hence more beneficial to the recipient charities.

It is in the context of managing stakeholder claims, however, that the content of this paper is unfolded. Brammer & Millington (2005: 31) suggest that 'philanthropy plays a significant role in establishing and developing favourable

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relationships with community stakeholders'. In seeking to examine and 'unpack' a specific example in which philanthropy appears to have been used to manage a particular potential community claim, this study shows how patterns of giving by British building societies in the late 1990s were consistent with the need to enhance community profile to reduce the threat to their mutual status arising from pressures to demutualise. This, we argue, was a strategic threat to building societies in that it had the potential to change the legal form and financial structure of the organisations themselves.

In this paper, giving data for 31 building societies over a 14-year period are examined, along with the media attention (and hence public awareness) given to the demutualisation issue and the commentary of building societies on the geographical distribution of their giving. These findings are supplemented with evidence from the Director-General of the Building Societies Association (BSA) to enrich the analysis of the situation at the time of the observed change in giving behaviour. The paper concludes that giving was used in a highly instrumental way at the time of the maximum threat to their mutual status, which is, in turn, interpreted as evidence for the strategic use of philanthropy. This represents the first analysis of giving behaviour in response to a specific community claim in a single sector and as such, may inform future studies in this area.

The remainder of this paper proceeds as follows: in the next section, the current literature on philanthropy, and more specifically strategic philanthropy, is covered, followed by a discussion on the nature of building societies and the issue of demutualisation. The paper introduces two research questions for which the research method is subsequently described. The findings are presented and finally, a discussion is entered into that interprets the findings as evidence for an instrumental and strategic use of charitable giving in this case.

Corporate philanthropy and strategic philanthropy

There is a growing literature on the subject of corporate philanthropy. The prior work can be broadly, if crudely, divided into three types. The first type seeks to probe the debate over the economic and moral cases for and against philanthropy (Friedman 1970 (obliquely), Shaw & Post 1993, Campbell *et al.* 1999, Dean 2001 and the broad discussion in Burlinghame & Young 1996). The second type are those that have sought to investigate the relationships between levels of philanthropy and specific firm characteristics. These studies have examined a number of potential variables associated with levels of philanthropy that include *inter alia*, board composition (Wang & Coffey 1992, Williams 2003), firm size (Adams & Hardwick 1998, Seifert *et al.* 2003), industry structure (Brammer & Millington 2004) and firm visibility (Brammer & Millington 2006, Campbell & Slack 2006). The third type are those that have conducted empirical analysis of longitudinal, cross-sectional and international patterns of giving behaviour (Campbell *et al.* 2002, Brammer & Millington 2004).

An emerging genre of work relating to corporate philanthropy concerns its use as a part of the overall strategy and strategic positioning of a company. In an early contribution, Haley (1991) discussed charitable contributions in terms of 'social currency' and suggested that contributions can be and are used to 'align corporations and environments' and can serve as 'strategic resources' (p. 485). She proceeded to suggest, without offering supporting evidence, that contributions might be used, 'to influence corporate stakeholders, to shape society and to advance managerial interests' (p. 486).

It is clearly possible for donations to serve corporate interests over and above the purely altruistic and a number of studies have found or examined such possibilities. The notion that philanthropy can be used strategically is one that has been explored by Smith (1994), Post & Waddock (1995), Saiia (2001), Porter & Kramer (2002), Saiia *et al.* (2003) and Seifert *et al.* (2003, 2004). Saiia *et al.* (2003) suggested that charitable donations can be used as a part of the overall strategic positioning of a firm in its environment and found widespread use of strategic philanthropy in US companies. Further, the way in which donations can be targeted at particular causes, stakeholders or communities offers the possibility, they argued, for firms to use contributions as a means of fine-tuning strategic positioning with regard to particular stakeholder concerns. A specific example of this use of philanthropy is examined in this paper.

The study of strategic philanthropy is relatively recent in British academe (Post & Waddock, Saiia and Porter & Kramer all examined it within a North American context). In examining philanthropy within a British context, Brammer & Millington (2004, 2005, 2006) and Brammer *et al*. (2006) highlighted the use of philanthropy as part of stakeholder management. It was argued, for instance, that ‘philanthropic expenditures may play a significant role in stakeholder management’ (Brammer & Millington 2005: 29) and ‘charitable giving is an increasingly strategic activity that may play a significant role in the process of stakeholder management by enabling managers to show in a visible manner a commitment to a social agenda’ (Brammer & Millington 2006: 8).

In developing the empirical context of this paper, we now turn to the building societies themselves.

Conversion, ‘carpetbagging’ and demutualisation defences

The 1990s was a time of some change in the building society ‘movement’ in the United Kingdom (Stephens 2001). Driven in substantial part by directors and members seeking ‘windfall’ share allocations upon conversion to public limited status, a number of former building societies (which traditionally had mutual status[1]) converted to public companies by floating new issue on the London Stock Exchange. Although the first major demutualisation, Abbey National, occurred in 1989, the majority took place in the late 1990s. The modal year for conversions was 1997, with Alliance & Leicester, Halifax, Northern Rock and Woolwich all demutualising in that year. Bradford & Bingley converted in 1999.

The ‘wave’ of demutualisations was notable in social terms because the legal form of a certain type of organisation (mutual societies) was the subject of discussion in society in general. The prospect of often-substantial share windfalls precipitated discussion at levels of society traditionally assumed to be unacquainted with the complexities of business financing and legal form. Those building societies wishing to remain mutual had to defend themselves against claims by some members (mortgage holders and depositors) who ostensibly cared more for the prospect of a payout than the mutual future of the building society. The prospect of windfall payments for a token deposit value (typically £100) gave rise to the phenomenon of ‘carpetbagging’ where people joined multiple building societies in the hope of making a windfall if the societies later converted (Coles 1997).

Carpetbagging affected the whole of the building society sector, commencing in 1996. While some societies may have been specifically targeted following media rumours of conversion, carpetbaggers opened accounts with as many societies as possible in the hope of conversion and consequent windfall gains. Although individual societies were subject to different pressures, all building societies felt a threat, to some extent, from members, to convert. Carpetbaggers were, by and large, indiscriminate in their activities, investing in deposit accounts to thereby gain membership of the society and become the beneficiaries of subsequent conversion.

The *Independent* newspaper reported in April 1996 that

> speculators are stuffing cash into new accounts with building societies at a rate of £50 m a day as the scramble to open accounts and qualify for cash bonuses or share handouts continues . . . Nationwide, Bradford & Bingley, Britannia, Portman, Yorkshire and Coventry have all had an upsurge in new accounts . . . Leeds & Holbeck, Derbyshire, Cheshire and Chelsea have all raised minimum investment levels for new accounts. . . . Investors encouraged by media speculation have been turning their attention to Birmingham Midshires. (*Independent*, 17 April 1996: 16)

Similarly, the *Guardian* newspaper reported in June 1997 that

> hundreds of thousands of carpetbaggers besieged building societies this week in the search of free windfall shares. Nationwide was forced to close its doors to new customers after daily queues of 25,000 in its branches around the country. Almost every other society experienced similar queues as professional carpetbaggers flocked from society to society in search of free shares. Portman, Coventry and Yorkshire all raised minimum opening account balances. (*Guardian Money*, 21 June 1997: 6)

The *Sunday Times* reported (21 September 1997) that £5 billion was put into building societies over the three months from June to September 1997, which was more than the combined totals of 1992, 1993 and 1994, the predominant reason being carpetbaggers pursuing a conversion windfall.

For those societies seeking to remain mutual, this pressure presented a strategic challenge as it threatened to change the legal form of their business and would take control out of local communities and into the hands of return-maximising shareholders. The literature published by the building societies and their umbrella body, the BSA, around that time (mid to late 1990s) showed that mutuality defences were made using a number of practices and lines of argument. One of the arguments advanced was the claimed role of building societies in their local communities. In seeking to dissuade members from seeking demutualisation, it was suggested that building societies were socially contributive organisations and that conversion to public status would, in some cases, threaten this social contribution.

These claims are examined in this paper. In particular, one aspect of social contribution – the rate of charitable giving against profit before tax (PBT) – is analysed for building societies over the period of the demutualisation debate. Using media hits as a proxy for the intensity of societal debate over the issue, the way in which building societies responded to this debate using charitable giving rates is studied over the period 1990–2003.

Building society demutualisation

The public was made aware of the potential personal economic benefits of building society demutualisation with the conversion of Abbey National in 1989. The situation was described by Adrian Coles,[2] Director-General of the BSA.

> Abbey National converted in 1989 but the payout then was only £130 worth of free shares *[per member]* so that wasn't very much and *[then]* no one else converted for another 6 years. The big shock was the announcement by Cheltenham & Gloucester in 1994 that they . . . had agreed to be bought by Lloyds Bank and the average payout then was £2200. So that was unbelievable – you've opened a building society account for *[a deposit of]* £100 and, by the way, you've got some membership rights although you never knew you had them in the first place. *[Lloyd's Bank said]* . . . we'll buy those membership rights from you that you didn't know you had or were worth anything for £2200. People thought they were giving up nothing for £2200 and so that really shook up *[building]* societies . . . And that changed the whole tide of opinion. Societies had to work out, 'why do we exist?'

Donald Kirkham, the then chief executive of the Woolwich Building Society, made a similar comment as early as 1990: '[building] societies must have a clear sense of what they stand for, or they will face an identity crisis' (Kirkham 1990: 67). By the time that other large players in the building society 'movement' were preparing to convert in the mid 1990s, the building societies that had remained uncommitted or even expressed the wish to remain mutual came under pressure from some members to convert for the reasons alluded to in the above quotation. This precipitated the publication of a number of documents in which the remaining building societies wishing to remain mutual set out what they saw as the case for mutuality (some were called 'defence documents', while other discussions took place in regular building society newsletters and reports). These defences typically advanced two lines of argument. First, they pointed out the lower deposit to lending rate margins arising from the lack of a necessity to maximise profits and pay dividends to shareholders (Clarke 1998, Drake & Llewellyn 1998, although see also Boxall & Gallagher 1997). Second, it was typical to point to the social and community roles of building societies.

This second argument for mutuality was centred on the belief that some social or welfare objectives could be served through mutuality (Lewin 2002, Michie & Blay 2004). The basis of this logic was that in addition to their (in most cases) local presence (sometimes as specific as a suburb of a city) and hence local sense of accountability, mutual building societies were often better placed to serve local social needs than were public companies as they were less profit constrained and did not have the obligation to pay annual dividends. Boxall & Gallagher (1997: 117) put it thus: 'they [building societies] may be able to define altruistic objectives which win the support of their members; in that case, their behaviour would . . . differ from that of competing plcs'. Armitage (1991) and Tayler (2003) suggested that social benevolence might also attract customers to building societies and so further strengthen the argument against conversion. There is some evidence for a difference between banks and building societies in social attitudes. In respect of branch closures, for example, the Building Societies Service Activity Statistics 1995–2005 reported that between 1995 and 2003, banks closed one in five of their branches whereas building societies closed one in every 20.

Building society claims of social contribution

In May 2000, a Building Societies Association (2000) report entitled, 'The case for building societies' made the claim that (p. 10)

> many societies offer significant support for hundreds of local charities, sports leagues, employment initiatives and other community activities. Provision of community-based services and support *would be threatened* by conversion to plc status where the return to the shareholder is paramount and service to the customer secondary (emphasis added).

The report did not go on to explain how such support would be threatened but the reader was left with the impression that mutual status can be associated with substantial community participation and social contribution. A report entitled 'The mutuality and social responsibility report' (The Smart Company 2002, written for the BSA) suggested that (p. 2) mutuals 'have a core philosophy of community support and mutual responsibility'. In 1998, Adrian Coles, similarly, made reference to the social role of building societies and how this may have changed: '[They have] rediscovered the ethic that building societies exist to serve their local communities. Most societies provide assistance to a range of local charitable and community organisations' (Coles 1998: 178).

Discussions in a range of other forums in the 1990s and since sought to reinforce the impression that building societies considered themselves to be community minded and socially benevolent. The reason most often given for this was the absence of shareholders. This argument was advanced by a number of the building societies themselves.

The late 1990s was seemingly a time of some discussion in building societies about their place and positioning in local communities. In a document entitled 'It's your society, it's your vote' in 1999, Rhidian Jones, a member of the board of the Britannia Building Society (1999) (one of the largest), appeared to be suggesting that mutuality was associated with a higher level of community involvement than banks when saying (p. 12), 'I am acutely aware of the vital role that Britannia plays in the wider community . . . to keep Britannia part of your community, we must keep Britannia mutual'. Similarly, the smaller Leek United pointedly made reference to mutual status when describing an act of corporate benevolence: 'Leek United's community spirit is well known to all the pupils and staff at Blackshaw Moor School – they . . . [were given] computers for free, showing that mutuality can benefit not just Members, but the whole community' (Special general meeting papers 1999: 8). Further on, the Leek United board commented thus: 'Ceasing to be a building society could prejudice our role in the community, where we provide jobs and *support local good causes*'

(Special general meeting papers 1999: 13, emphasis added).

At the 1998 BSA conference, the then chairman John Heaps (who was also Chief Executive of the Britannia Building Society) spoke on these issues, saying,[3]

> in developing the argument against conversion, it was not enough for those societies to cling on to an obstinate refusal to recognise that the world may have changed, nor to stubbornly resist any change that might have an effect on their organisation. Instead they had to develop a coherent set of arguments that would enable them to advance the cause of mutuality with confidence . . . Mutuality matters because it offers links with the local community that other organisations envy.

Later discussion also seemed to reinforce the belief among building societies that mutual status was strongly associated with community involvement at a higher level than corporate status.

Some societies singled out charitable involvement for specific mention in explaining why they should remain mutual. The Newcastle Building Society, for example, made the following disclosure on its website saying:

> The Society also makes a sizeable [charitable] contribution. *It is likely that, due to the need for profit maximisation, we would have to withdraw from these* [charitable] *projects should the Society convert*. (www.newcastle.co.uk, accessed 12 December 2003, emphasis added)

Newcastle was not alone in conveying this message. Similar support for mutuality and the role of building societies in the community was demonstrated by the Nottingham Building Society.

> The record of mutual building societies, compared to banks, shows that building societies consistently offer better value products by putting 'people before profit'. This is a sound reason for Nottingham Building Society staying a mutual society and so continue to serve the best interests of its customers and the wider community for many years to come. The Nottingham is a community-based building society committed to the region it serves. (www.thenottingham.com, accessed 6 January 2004)

In order to explore the reasons underlying these beliefs, the question was put to Adrian Coles: Do you think that building societies have historically been more philanthropic/community minded than, say, banks?

> Yes I do, because building societies are based in localities. All [apart from two London-based building societies] are based outside of London, in communities, in little towns. The board is drawn from those communities, the senior staff and the junior staff – all the staff – are drawn from local communities. Whereas at the top of the big banks they're all based in the City [or] in Canary Wharf so the top people in building societies, even though they're obviously much smaller organisations than HSBC or Barclays are much more aware of the local community, much more likely to be nobbled by the local theatre trust or the local hospice, probably having much more of an open door anyway and [more] willing to be nobbled by those sort of people.

Research questions raised in this paper

Building societies appear, then, to have traditionally considered themselves to be differently positioned with regard to community concerns than corporate financial institutions such as banks. In that they are and were 'community based' (in the words of Nottingham Building Society) then it would follow that building society constituency profiles would be materially different from those of corporates. The importance of communities to building societies, in most cases – and especially to smaller societies – would be difficult to overstate. When the issue of potential demutualisation came onto the social and, importantly, community agenda, the management of local communities assumed an elevated importance to societies because communities not only had power over the long-term economic future of societies but also over the short-term future as a mutual organisation. When this mutual status was threatened, it became a strategic priority – for those wishing to remain mutual – to reposition themselves to meet the concerns and persuade mutuality agnostics of the case for mutuality. In the case of members based in local communities, the case was made, as described above, using both economic and social cases for mutuality.

This study seeks to interrogate the issue of the strategic use of philanthropy among building societies in two ways. In the first instance, evidence is sought on the behaviour of the building society sector as a whole to the issue of the potential member claims upon it with regard to demutualisation. Second, it seeks to examine the giving behaviours of individual societies where possible (i.e. where evidence was available) for a greater understanding of how individual societies within the sector behaved in the use of philanthropy to further strategic ends. Comparative giving data against the cohort of UK-based public status banks are also included in order to demonstrate differences in giving behaviour over the key period of the study.

The richness of the analysis offered in this paper over and above alternate approaches like statistical cross-sectional analyses rests upon the interrogation of both the above questions. To address them meaningfully, it was necessary to adopt a mixed method using elements of several different research approaches. The next section discusses these.

Sample and method

In order to address both research questions, it was necessary to measure meaningfully giving behaviour for individual societies and for the sector in general. To contextualise the study, giving rate statistics for the building society sector were also compared with those of the banking sector in order to highlight any significant trend variation between the two groups. Finally, evidence on the changing pressure from communities on the issue of mutuality and on the specific nature of building society community involvement is discussed (using the proxy of newspaper 'hits'). This community pressure was measured in terms of pressure on the entire building society 'movement' and on selected named individual building societies.

Building society sample, banks and charitable giving data

The narrative from the building societies, the BSA and other entities has used a number of terms to describe their general approaches to social and charitable involvement and contribution: 'social responsibility', 'community support and mutual responsibility', 'part of [the] community', 'community spirit', 'benefit the community', 'support to the communities', 'best interests of ... the communities we serve'. Although charitable donations comprise only a part of an organisation's potential engagement with their communities, they offer the advantage of accurate measurement along with the potential for longitudinal and cross-sectional comparison. It was a requirement throughout the period of the study described in this paper to disclose the cash amount given to charity[4] and, in keeping with building societies' reporting regulations reflecting aspects of UK company law, the specific mandatory disclosure of pre-tax profit allowed for a convenient comparison of the two to be made: the giving rate or, as referred to by Campbell *et al.* (2002), the 'generosity ratio'. Charitable donations also offer the advantage (which is central to the motivations examined in this study), for donors, to demonstrate community concern in a tangible and visible manner. By, say, endowing a charitable foundation, supporting a local youth cause or performing similar acts of community support, any claims of community support can be amply demonstrated. Such a demonstration would be more difficult with other types of social contribution.

Calculation of giving rate required obtaining the actual giving figure and the PBT (both in currency units) for each society and for each year of the study. This necessitated the examination of the annual reports and accounts of the mutual societies between the sample years of 1990 and 2003. The sample of building societies was 31 (from the total of 65 remaining societies). When aggregated, these 31 societies comprised 94.5% (2002 figures) of the total asset value of the building society 'movement' and so adequately represented an indication of total giving rates over the period of the study. The same data were collected from all of the United Kingdom 'high street' or retail banks so that a comparison could be made between these two financial sectors to show the effects of building society giving rate changes against the banking sector. This comprised charitable donations and PBT for the seven major retail banks (listed on the London Stock Exchange) that had been public companies for the duration of the study.

The majority of the data collection was conducted using hard copies of the annual reports of the building societies using the library of the BSA in London. Hard copies of all listed bank annual reports were also used.

Measuring societal attention to the issue of demutualisation

Prior studies in some other areas of academic enquiry have used media attention to an issue as a proxy for the intensity of concern for that issue more generally. In order to address the first research question (concerning the way in which the building societies *as a sector* responded to the demutualisation issue), it was necessary to gain a measure of the intensity of concern that existed among communities about the demutualisation issue.

Prior studies have used a number of ways of using proxy data to measure the intensity of societal concern for, or interest in, an issue. In gauging the strength of opinion in society on the issue of concern for the natural environment, Deegan & Gordon (1996) and Campbell (2004) used environmental lobby group memberships over time. This was then correlated against the amount of environmental disclosure in company annual reports over the same period to establish the extent to which companies were responding to environmental concern in society. A more common approach has been to use a measure of media attention to an issue on the premise that the frequency of media discussion of an issue (say in a given year) is a fair measure of the intensity of society's discussion of, or concern over, that issue at that time.

Brown & Deegan (1998) used this approach when seeking a proxy for the intensity of general social concern on, in their case, environmental issues. Selecting a time period over which media hits were obtained from an Australian business index of seven newspapers, a number of keywords were used to identify newspaper articles discussing issues associated with the environment. The number of articles per year was taken as a proxy for the intensity of societal interest in the environment at that time. Using such a technique, it could be possible, when no other information was available, to establish trends in interest in a number of potential issues discussed in print media. One might think, for example and hypothetically, of 'Watergate', 'Vietnam' or 'Enron'. In each case, a longitudinal record of media hits would be likely to highlight the peak of interest in the item and the waxing and waning of interest either side of the peak. A similar approach was adopted to measure the intensity of interest in building society demutualisation and hence, by proxy, the need for building societies wishing to remain mutual to take defensive measures.

In developing what became known as 'media agenda setting theory', Brown & Deegan (1998) proposed a causal relationship between media discussion of an issue and corporate behaviour where it pertains to that issue. Basing a media hits analysis at two- and three-year intervals in seven Australian newspapers over 13 years, Brown & Deegan found an association between media attention to environmental concerns and environmental disclosure by affected companies. Erfle & McMillan (1990) used a media coverage method based on mentions of given companies in television news programmes. Brammer & Millington (2006) used a news hits measure to proxy public visibility.

The news hits data for this study were gathered using the search feature on LexisNexis, an online source of narrative from a large range of daily and weekly regional and national newspapers. In order to ensure internal consistency of data, a number of filters were applied to the selected publications to be used in the media hits capture. First, to control for regional bias, only national newspapers were selected. Second, any national publication unable, for reasons of membership of the LexisNexis database, to report over the full-longitudinal period of the study, was excluded. This, surprisingly, included some relatively established national titles including the *Daily Telegraph* and the *Daily Express*. Finally, all mainly financial newspapers, notably the *Financial Times*, were excluded as it was assumed that discussions in these newspapers, unlike in national papers as a whole, may reflect discussion by capital market participants rather than in society as a whole (this being a prominent motive in using the media hits method). The application of these filters produced a list of seven qualifying newspapers: *Observer*, *Sunday Times*, *Mail on Sunday*, *Daily Mail*, *Guardian*, *Independent* and *Times*. Although the list of newspapers is not exhaustive, it should be borne in mind that the purpose of the data hits exercise is not to find all media hits but to describe the trend in relevant hits over the years in question.

Two separate interrogations of the newspaper archive were made. In order to establish the total number of media 'hits' referring to building societies *in general* and demutualisation, two interrogations of the archive were made. In the first, three terms were used to arrive at the article descriptor: 'building societ*' (using a wild card to allow for the latter word to read 'society' or 'societies'), 'conversion' and 'demutual*' (wild-card to allow for 'demutualise', 'demutualising', 'demutualised' and 'demutualisation' and the plural and 'z' forms of these). In the second, the search specifically sought reference to building societies and 'carpetbagg*' (again, using a wild-card). The annual frequency of these articles became the proxy used in this study for the intensity of public debate on the subject in question. The second interrogation was intended to establish the media attention given to selected individual building societies with respect to the demutualisation threat. For this interrogation, articles were selected containing the words 'carpetbagger' or 'carpetbagging' and the name of the society in question (e.g. 'carpetbagg*' and 'Britannia').

Other methods used

In developing the content for this paper, the authors were fortunate to be able to discuss its contents with the Director-General of the BSA, and some of his thoughts are used in this paper. The evidence on the proximity of charitable donations to operations and/or branches was gained from analyses of society documents (such as annual reports) or the relevant sections of society websites. Evidence from these components is introduced in the discussion section below.

Findings

News hits

The number of news hits per year (i.e. those articles in the selected newspapers containing all three search terms) is shown in Table 1 and as a graph in Figure 1. Interest in the early 1990s was confined to consideration of the early converters (mainly Abbey National) and the possibilities of others converting. When other large societies announced their intention to convert or actually did so, the attention paid by the press increased

Figure 1: Media hits by year (the data in Table 1)

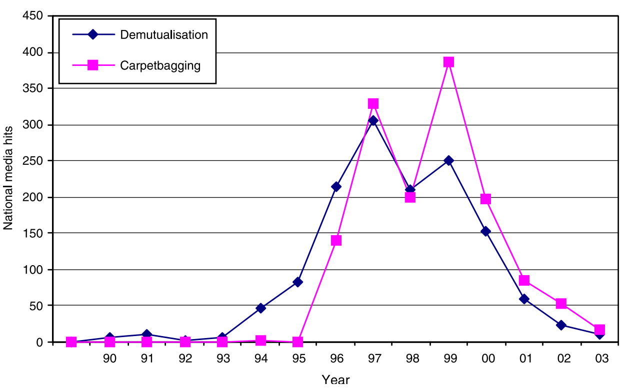


Table 1: Frequency of news hits by year (1990–2003)

Year	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Hits (A)	7	10	2	7	46	82	215	305	210	251	153	60	23	11
Hits (B)	0	0	0	0	2	1	140	330	200	387	198	85	53	18

Incidence of selected terms in *Observer*, *Sunday Times*, *Mail on Sunday*, *Daily Mail*, *Guardian*, *Independent* and *Times*. Hits (A) captures the terms 'building societ*', 'conversion' and 'demutual*'. Hits (B) captures 'building societ*' and 'carpetbagg*'.

Table 2: Correlation statistics (1990–1997) for selected building society giving rates against media hits

	Britannia	Coventry	Cheshire	Newcastle	Nottingham
Multiple R	0.96	0.68	0.79	0.79	0.98
R^2	0.93	0.47	0.62	0.63	0.96
R^2adjusted	0.92	0.38	0.56	0.57	0.95
Standard error	33	90	76	75	25
Observations	8	8	8	8	8

accordingly. The peak of discussion was the modal year for demutualisations: 1997. A second, smaller peak in 1999 coincides with the demutualisation of Bradford & Bingley Building Society.

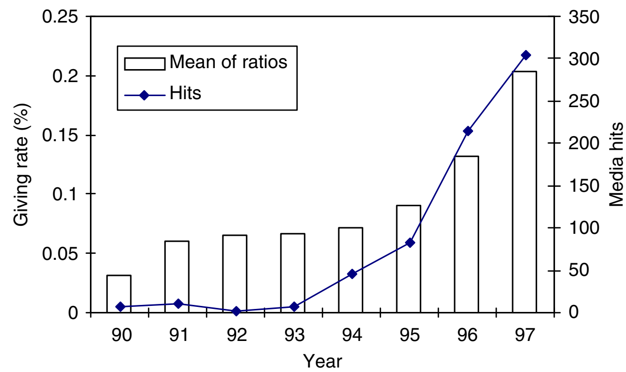
The shape of the line in Figure 1 clearly shows the effect of demutualisation, and carpetbagging, that affected the sector, being a topic of interest for a season of several years but with little or no such interest beforehand or afterwards. This suggests that the intensity of societal discussion on the issue of demutualisation was probably ephemeral and lasted for several years with a peak over 1997. By 2001, there was evidence of a substantial diminution of interest. Note also how the term 'carpetbagger' entered the public vocabulary (with regard to building societies) only in 1996, some years after the discussion about conversion began.

For individual society news hits, the number (frequency) was, predictably, lower than for the total figures. The largest societies by value were the most mentioned in the press. The figures for selected individual societies are shown in the Appendix. In most cases, a trend similar to the total sector hits frequency can be noted. With the first one-off mentions in 1994 and 1995, it seems to have suddenly appeared as a media issue in 1996. The media hits data for individual societies were correlated against the individual societies' giving rate records over the same period. The results are shown below.

Giving rate correlations – total sector news hits

Table 2 shows the high correlations of giving rates against media hits ('Hits A' – from Table 1) that were noted for some of the building societies over the years 1990–1997, which were the years of

Figure 2: Mean giving rate for building societies by year and media hits by year. Adjusted $R^2 = 0.91$ (significant to three decimal places). The graph shows the correlation over the key period 1990–1997



rising interest in the issue of demutualisation in the newspapers. Although these high-correlation figures were not noted in all cases, the majority of building societies substantially increased the rates at which they gave to charities over the period. Figure 2 shows the mean of the 31 building society giving rates by year against the media hits frequency data shown in Table 1 over the same period, 1990–1997. The adjusted R^2 of this correlation was 0.91 (significant to three decimal places). Adding two extra years (1998 and 1999) and calculating the giving rate by dividing the sum of all donations by all profits for a given year produces a lower correlation ($R^2 = 0.48$), although a general and approximately coinciding shape can be discerned in both variables described.

When the years after the peak of 1997 are included (Figure 3), a slightly different picture emerges. While (as we noted in Figure 1) the media hits returned to a low level (a handful of hits per year), the rate of giving for the sector as a whole, measured by mean giving rate of the

Figure 3: Mean giving rate for building societies by year and media hits by year (1990–2003)

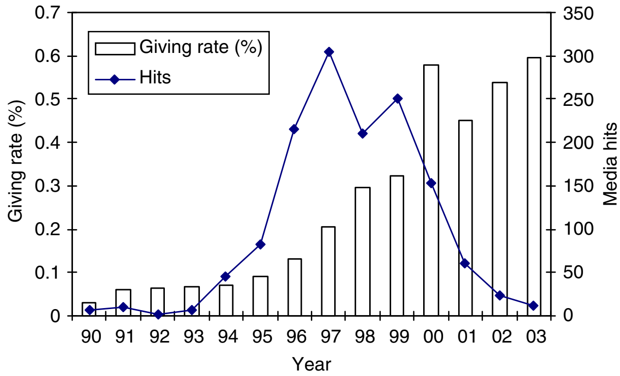
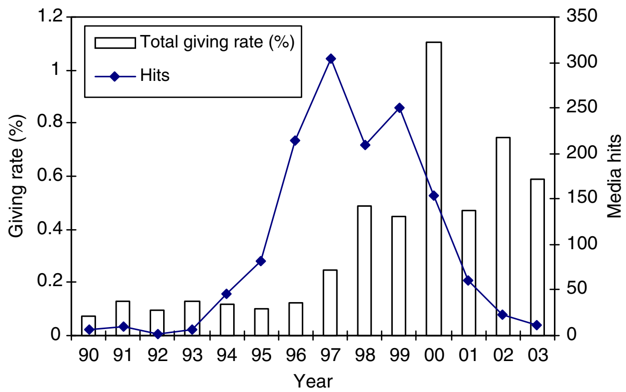


Figure 4: Giving rate calculated as total giving divided by total profit before tax (PBT) (ΣDonations/ΣPBT) for building societies by year (expressed as percentage) against media hits for the years 1990–1999. Multiple $R = 0.61$, $R^2 = 0.48$

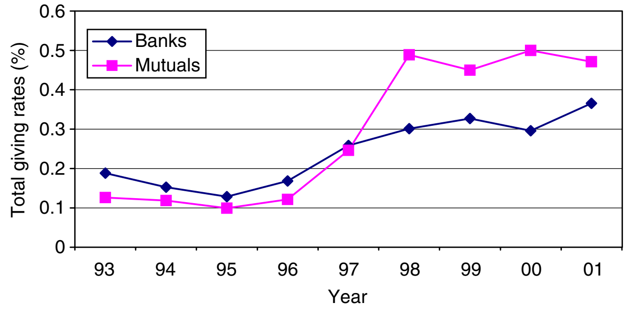


31 remaining societies, levels off at approximately the peak figure that it reached in year 2000 (Figure 3).

A similar picture can be seen when the total giving divided by the total PBT for the sector, by year, is calculated (Figure 4). This calculation, which smoothes out large or small individual society giving rates, is an expression of the giving of all 31 building societies together in a given year.

$$\text{Total sectoral giving} = \frac{\sum \text{donations for building societies}}{\sum \text{PBT for building socities}}$$

Figure 5: Total sector giving rates (ΣDonations/ΣPBT for mutual societies and banks). Years 1993–2001 to show changes over key period of study.



It shows an 'off-trend' peak in the year 2000 but otherwise a levelling off at a higher level than previously at between 0.5% and 0.7%. Correlation calculations for the data shown in Figure 4, between the years 1990 and 1999, show an R value of 0.61 ($R^2 = 0.48$) but this figure rises as the two variables are brought closer together by lagging the news hits. A three-year lag produces $R = 0.9$ and an R^2 of 0.8. This may indicate some frictional response by the building society sector to the rising media hits and hence rising intensity of discussion in society.

Figures 3 and 4 both show a marked increase in giving by the building society sector commencing in 1997 and continuing through to 2000 before levelling off thereafter. In order to investigate specific issues surrounding the building society sector that could have contributed to this change, giving data of the building society sector were compared with the United Kingdom retail banking sector (as explained above). This is shown in Figure 5 and focuses on the years surrounding the key period of the study from 1993 to 2001 (see also Campbell & Slack 2007). This shows a marked increase in giving of building societies when compared with banks during 1997–1999, suggesting a specific building society factor that led to such a change. A more general (non-sector specific) societal or economic pressure to increase rates of giving would have led to a general increase in rates across both sectors. In the earlier years, 1993–1996, the total giving rates of the two financial sectors were comparable and it is only from 1997 onwards that significant divergence occurs, shown by a clear upward shift of building society giving.

Giving rate correlations – individual society news hits

This section examines the ways in which individual societies responded to media attention about them individually. Given the small number of hits that most individual societies 'scored' in the press, this exercise was not meaningful for many of the societies. Where the number of hits was large enough to allow for significant findings, regressions were calculated against those individual societies' giving rate records over the years 1990–2000. The findings are shown in Table 3, which also shows the correlation statistics for those societies' giving rate records against the total media hits data ('Hits A' from Table 1) used in the above section of the paper.

Table 3 shows that while some individual societies appear to have responded strongly to media attention *about them* using giving rates, the correlations are not consistently higher than correlations between those societies' giving rates and the total media hits data relating to the building society sector in total.

The correlating effect over the years 1990–1997 is further shown in Figures 6a–f where the changes to giving rates for a number of selected building societies are analysed against, in each case, the total media hits data described in Table 1 ('Hits A').

It is noteworthy that despite the appearance of an increase in giving around the time of the later 1990s, not all giving rates were equally high. Whereas (based on the graphs shown in Figures 6a–f) Nottingham Building Society's giving rate increased to over 1% of pre-tax profit, for others, the rates remained very parsimonious. Most building societies remained below the giving rate of 0.5% of pre-tax profits expected from Percent Club[5] members.

Discussion and conclusion

This paper set out to examine the motives for giving in the building society sector over an important period in which the legal status of many mutual societies was threatened. In seeking to find defences against the threat of demutualisation, this study found evidence in support of the belief that charitable donations may have been used as a part of the fine tuning of strategic positioning with respect to a particular constituency – its members, often based in local communities, who, collectively, have power to determine the legal status of a given building society.

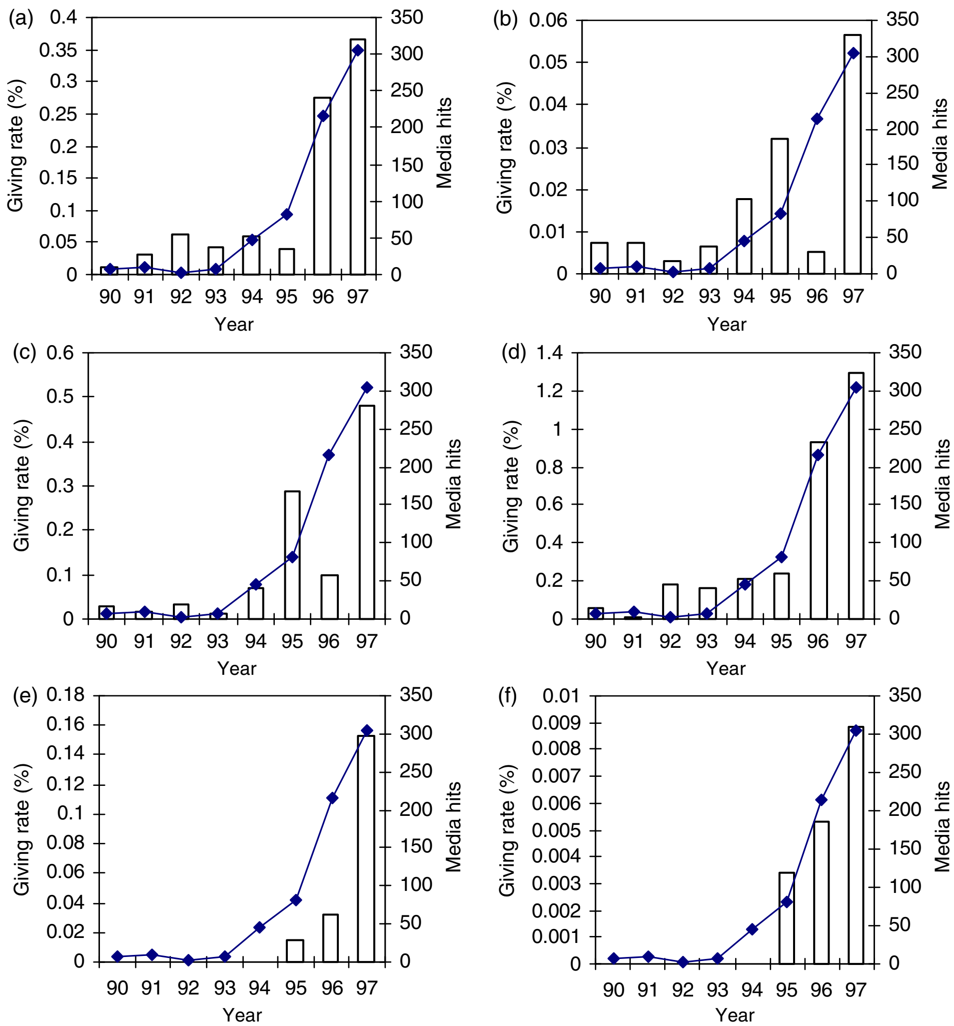
The evidence from the associations between media hits and sector-wide giving rates suggests a

Table 3: Regressions for selected societies' giving rates against media hits relating to general issues of building society demutualisation ('total hits') and against national media hits relating explicitly to the society in question and carpetbagging

	Multiple R	R^2	Adjusted R^2
Britannia GR vs. total hits	0.80	0.64	0.60
Britannia GR vs. Britannia hits	0.67	0.45	0.40
Yorkshire GR vs. total hits	0.64	0.41	0.35
Yorkshire GR vs. Yorkshire hits	0.86	0.75	0.72
Portman GR vs. total hits	0.42	0.17	0.08
Portman GR vs. Portman hits	0.83	0.68	0.65
Cheshire GR vs. total hits	0.72	0.52	0.47
Cheshire GR vs. Cheshire hits	0.88	0.78	0.75
Leek GR vs. total hits	0.87	0.75	0.72
Leek GR vs. Leek hits	0.69	0.47	0.41

Note. In all cases, regressions are calculated for years 1990–2000 inclusive. GR, giving rate; and 'hits', the number of media articles, all by year.

Figure 6: Illustrations of associations between giving rates in individual societies and media hits. In all cases, media hits is the line and giving rates (as percentage) is the bar. (a) Britannia. (b) Coventry. (c) Cheshire. (d) Nottingham. (e) Leek United. (f) Derbyshire



concerted response by building societies to the intensification of societal discussion of demutualisation. Before the mid 1990s, it would be difficult for building societies to support the proposition that they were benevolent towards their communities if the rates of charitable donations were the measure. Many societies gave nothing at all and others gave very small amounts, often only a few hundred pounds a year. The fact that all 31 of the societies analysed in this study increased their giving during the mid 1990s – and in many cases dramatically so – suggests a structural change in posture towards charitable giving at that time. The fact that the building society sector was responding to a specific factor is further evidenced by a comparison with giving behaviour by public status banks over the same period. This showed a marked increase in relative giving by the building society sector in comparison with the banks between 1997 and 1999.

The purpose of building societies from the early stages of their development was as 'thrifty' institutions: ones in which any surpluses would have been used for the direct support of members through preferential lending and borrowing rates rather than through donations or dividends to shareholders (as there were none). Hence, while it is perhaps unsurprising that donations were initially at a low level, it must have been a notable series of events that perturbed the sector from its prior giving behaviour. The issue of the threat of demutualisation was such a perturbation and seems to have been responded to when the legal status of the sector as a whole underwent increased societal scrutiny and when individual societies received increased media attention.

The question was put to the Director-General of the BSA: While mutuals have always had this . . . 'historic' local relationship [with communities] because of where they're from, [after] 1997 was there a need to make this much more demonstrable?

> *Answer:* Absolutely right . . . the ones that remained [mutual] said, well, we've got to distinguish ourselves here. We've got to be different and after a period of soul searching the remaining building societies said look, we give you pricing benefits, we give you benefits of service . . . we are part of the community . . . we are different from the banks.

Question: But your perception is that in the late 1990s, societies did all of a sudden wake up to how to give an appearance or show their community involvement. Can you give examples of that?

> *Answer:* I think more time spent by the [building society] chief executives on local initiatives. [One such building society chief executive is] Chairman of [his] local city centre regeneration partnership, he's on the Board of a local theatre . . . Now that would have happened in the past but is probably happening more now. The involvement of staff with schools and housing associations for example [has] been given a bigger push.

Question: So did they [building societies] become demonstrably more visible in their relationship or engagement with the community?

> My assertion would be yes.

It appears from the data shown in Figures 3–5 that three distinct phases of giving behaviour can be observed. In the first phase, from 1990 to 1995 or 1996, the rates of giving were very low, and in some cases, non-existent (possibly for reasons of their purpose of 'thrift' described above). Whereas other sectors of the economy were giving at this time, often at substantial rates against profits (Campbell *et al.* 2002), building societies seemingly saw no such need. In the second phase, the three-year period from 1996 to 1998 (inclusive), there was a concerted increase in giving to a multiple of previous levels. The third phase, from 1999 to 2003, is characterised by a return to a relatively consistent level of giving, but at the elevated level resultant of the increase observed in the second phase. In this regard, the change in giving behaviour over the period studied is sigmoidal in shape.

It is difficult to explain such a concerted increase in giving by members of an entire sector as anything other than relating to a common cause. This article posits the view that the observed increase in giving and the changes in media hits discussing demutualisation are related. In order to support the proposition that individual societies acted strategically in increasing their giving to respond to community threat, it is necessary to examine the situations of individual societies.

With regard to smaller societies, the Director-General of the BSA made the following remark.

> The smaller societies also faced [pressures to demutualise] and they wanted to engage with the local community to make sure that the local community realised that it wasn't just free shares. They'd get free shares, perhaps, if the society converted, but [they would] lose better pricing. [Demutualised building societies might be forced to] close branches and the boys' local football league, the horticultural society, the local theatre also would not be sponsored.

It is the manner in which charitable giving was directed at principally local (to the giving society) community and charitable causes that provides further evidence for the strategic and instrumental use of giving in this case. It is because many building societies are small, with members concentrated in a particular geographical area, that giving has the potential to be highly targeted at member communities than is likely to be the case from larger national or multinational companies.

There is ample evidence that individual societies privilege local (to themselves) causes over others when it comes to the distribution of charitable and community donations.[6] The Britannia Building Society, through its charitable foundation, specifies its area of interest to be, 'within a 25-mile radius of its Leek [Staffordshire] headquarters'. Leeds Building Society specifies that, 'the project [supported] must operate in the area of one of our 57 branches'. The Nottingham supports causes from 'communities within our branch area', Newcastle uses the terms, 'areas surrounding our branches' and 'in areas where we have a branch presence', while the Coventry refers to 'the region covered by Coventry Building Society's branch network'. There is no evidence that any of the building societies sponsored larger, national causes and the reason for this is, we suggest, that such support would not help the building society in relating to the specific communities it needed to curry favour within its strategic purpose to remain mutual.

It was the members who had the power to force a vote on demutualisation and so it was they and their expectations, specifically, that needed to be 'managed'. It seems that the use of charitable donations were, and possibly remain, a central component of the management of member expectations and demands, especially those regarding support for the continuation of the building societies in their mutual legal form.

It is this analysis that represents the contribution of this paper. At a time of unprecedented threat to their legal status as mutual societies, building societies, collectively and individually, recognised their need to manage their community constituencies to discourage any pressure to demutualise. As a sector, the increase in giving was dramatic and closely followed an equally sudden increase in societal attention to the issue of demutualisation as proxied in the media hits measures (Table 1). Individual societies also showed evidence of sudden and dramatic increases in giving and evidence that what giving there was, was targeted at communities in close proximity to the branches, demonstrates the strategic purpose of giving in those cases.

The opportunities for further research arising from these findings are relatively self-suggesting. A method involving engagement with the individual building societies for the purposes of gaining insight into the discussions that took place at the time may yield interesting findings. Such a method would not be without issues, however, as, in addition to the usual problems of gaining access at the strategic level, the main debate over demutualisation took place almost a decade ago and those who participated in discussions at that time may have moved on or retired.

Acknowledgements

The majority of the data collection for this study was conducted in the library of the BSA in London. The authors would like to thank the BSA for this access and in particular, Simon Rex, for his adroit stewardship of the library and his help on the several visits the authors made. The paper would be substantially poorer without the inclusion of the contextualising and explanatory comments made by Adrian Coles, the Director-General of the BSA, and the authors would like to thank Adrian for his interest in the project and the time given to be interviewed. Chris Cowton provided helpful feedback on an earlier version of the paper and Claire Tobin transcribed the interview with Adrian Coles.

Notes

1. A society jointly (mutually) owned by its members (depositors and borrowers) and run on a co-operative basis for the benefit of its members rather then third-party stockholders. Most building societies were initially locally based (hence their names), and established and operated for the benefit of industrial workers in those localities.
2. All excerpts from Adrian Coles are verbatim from an interview held on 21 October 2005. The authors are grateful to Mr Coles for the interview and his agreement to be quoted 'on the record' in this paper.
3. Text of a speech by John Heaps, Building Society Association conference, 3 September 1998.
4. Thanks to Chris French of the Building Societies Association for clarifying this. Under UK company law, this disclosure has been mandatory since the Companies Act (1967) and it became a requirement for building societies at some point after that. In all cases, the requirement is to disclose the cash amount in the Directors' Report, a component of the annual report and accounts.

5. The Percent Club is part of Business in the Community. Its members undertake to give at a preset rate against profit every year, normally 0.5% although some undertake to give at 1%.
6. All quotations are taken from building society websites, examined in November 2006.

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Appendix

Table A1: Media hits data for the term 'carpetbagg*' and the name of the society in question

	Nat'wide	Yorkshire	Chelsea	Skipton	Portman	Britannia	Coventry	Cheshire	Leeds	Nott'ham	Stroud	Leek	Derbyshire	Camb'ge
1990	0	0	0	0	0	0	0	0	0	0	0	0	0	0
1991	0	0	0	0	0	0	0	0	0	0	0	0	0	0
1992	0	0	0	0	0	0	0	0	0	0	0	0	0	0
1993	0	0	0	0	0	0	0	0	0	0	0	0	0	0
1994	0	0	1	0	0	0	0	1	0	0	0	0	0	1
1995	1	4	2	0	0	0	1	0	4	0	0	0	1	2
1996	28	14	8	9	17	26	6	3	26	2	3	1	0	2
1997	214	35	26	34	39	63	27	7	13	5	1	0	5	10
1998	133	38	14	10	15	37	19	6	7	3	1	3	5	8
1999	179	118	91	88	102	147	69	10	59	10	5	45	6	1
2000	62	27	71	57	46	18	10	4	16	2	0	5	13	4
2001	65	3	30	2	29	7	5	1	4	1	0	2	3	0
2002	40	6	12	8	13	20	1	3	0	2	0	3	1	1
2003	8	4	2	1	5	2	1	2	3	1	1	3	2	3
Total	730	249	257	209	266	320	139	37	132	26	11	62	36	32

Publication 5

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Employee involvement in corporate philanthropy: informing company policy, reputation management and employee motivation.

Refereed paper

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Keywords: Philanthropy, Employee, Involvement, Disclosure, Policy

Abstract

Charitable giving by businesses forms an integral part of Corporate Social Responsibility strategy and practice. This research examines the extent to which employees, as a stakeholder in business, are involved with the giving decision such as choosing or nominating the recipient charities. Involving employees to inform such policy explicitly recognises employees as a stakeholder group with decision making importance and could be used to enhance employee morale and their social relationship with the business contributing to increased employee retention, motivation and recruitment.

Companies face increasing pressure for greater transparency and accountability and accordingly this research examines the policy disclosure to stakeholders, informing them of charitable donations. By combining employee policy involvement and transparency of disclosure, this research draws upon agency and stakeholder theories and enables comment on the influence accorded to employees within a social area of the business and its benevolence to society.

The research objectives are as follows:

- To examine the extent of philanthropic policy disclosure by FTSE100 companies,
- To identify those companies where employees are involved in policy making and examine their contribution to policy,
- To examine the descriptive reporting of philanthropy by companies and the general level of employee involvement.

The research is conducted by examining the charitable donations disclosures within the annual reports of all FTSE100 companies for the year ended 2006. Despite the widely recognised benefits of philanthropy, the findings reveal disparity of reporting concerning the disclosure of philanthropy policy and the extent of employee involvement in such policy areas which raise questions of agency and stakeholder management. Whilst most companies include employees in their general reporting narrative of charitable activities there remains a question as to why all companies do not engage employees in their philanthropy policy formulation.

‘The Group believes that commitment to corporate responsibility delivers competitive advantage

> We encourage the giving of donations to charities which support the global communities in which we conduct business
>
> We attract and retain the best people’

Rolls Royce Annual Report 2006 (page 38)

Introduction

There is a steadily growing academic literature on issues surrounding corporate charitable donations. Public interest in the subject has also been raised in recent years with the introduction (in 2001) of the Guardian ‘giving list’ where companies are ranked according to the value of their cash and in-kind donations. A small number of organisations exist to study and encourage corporate charitable involvement with Business in the Community and its subgroup, the PerCent Club, being the most prominent.

In addition to the questions of *how much* is given by businesses to charity and community causes (typically calculated as a proportion of profit before tax), are the more difficult *why* questions. In this area, complex questions of motivations have been considered and these are supported in part by the debates in the management literature about the nature of the relationship between business and society (Donaldson and Preston, 1995; Suchman, 1995). Dual purposes and benefits of corporate philanthropy can be advanced; an external focus on reputation and impression management (Brammer and Millington, 2004a) and an internal focus on employee motivation, recruitment and retention (Brown, Hellard and Kiholm Smith 2006). The external and internal benefits of such philanthropy are not mutually exclusive and serve to enhance the business from a multi stakeholder perspective. This was explicitly recognised within McKinsey Quarterly (2007) that found that enhancing corporate reputation, building employee capabilities and improving employee recruitment and retention were the three most cited business goals arising from corporate philanthropy programmes. Two associated theories serve to underpin the development of the study. Agency theory is used to explain the need for philanthropy policies so as to inform shareholders and other stakeholders, such as employees, about the donations of large amounts of money to charitable causes. By providing such policy disclosure companies are discharging their accountability to their stakeholders. Secondly, stakeholder theory is used to recognise the role of wider stakeholders in policy decision making and the internal as well as external motivations for corporate philanthropy. This addresses employees as a key stakeholder in the business.

Corporate policy on charitable donations and, more specifically, the involvement of employees in such policies has been a less-explored line of inquiry in a growing literature on charitable donations research. The sums of money donated by some companies can be relatively substantial, for example £41 million by Vodafone and £37 million by Lloyds TSB in 2006. Overall charitable giving by FTSE100 companies for 2006 was £362 million, with wider CSR donations totalling nearly £1 billion[1]. However, despite these amounts, little is known about what policies or decision-making processes involving employees may be in place to guide such giving. Brammer and Millington (2005) recognised the need for greater research surrounding employee involvement and philanthropy. This study seeks to address this by examining policy disclosure policies and the involvement of employees in

[1] All figures from The Giving List, published in The Guardian, 6 November 2006

philanthropy. It also examines the potential benefits of such involvement, whilst at the same time recognising that there may be a difference between policy disclosure and policy-in-action.

The research objectives are as follows:

- To examine the extent of philanthropic policy disclosure by companies,
- To identify those companies where employees are involved in policy making and examine their contribution to policy,
- To examine the descriptive reporting of philanthropy by companies and the general level of employee involvement.

This study seeks to inform the issue of charitable donations policy disclosure by drawing in part upon method and literature from voluntary disclosure studies. In seeking to establish the extent to which UK companies have published charitable donations policies and the content of such policies, content analysis was conducted on FTSE 100 companies' annual reports for the year ending 2006. Using a coding instrument capable of resolving different types of disclosure pertaining to charitable donations, the study set out to establish the extent to which predetermined policy underpinned UK charitable donations activity, the involvement of employees in any such policies and the general use of employee narrative in corporate philanthropy disclosure.

The remainder of this paper proceeds as follows. In the next section, the literature on charitable donations and employee involvement is reviewed. Whilst there is a substantial literature on employee involvement this study seeks to link corporate philanthropy with employee involvement and hence employee issues pertinent to that link are covered. Arising from the literature and the overall aims of the study, four hypotheses are then presented. The method is then described and, linked to that in the context of this study, is a brief discussion of issues in content analysis. Finally the findings are presented and discussed.

Previous corporate philanthropy and associated employee literature

The literature on corporate philanthropy can be broadly considered to comprise a subset of the more general literature on corporate social responsibility, reporting and performance encompassing social and environmental accounting issues (Solomon and Solomon 2006; Miles, Hammond and Friedman, 2002; Richardson, Welker and Hutchinson, 1999, Balabanis, Phillips and Lyall, 1998 and Preston and O'Bannon, 1997). Among those papers that have specifically explored aspects of charitable donations activity, three general research themes can be identified; moral and economic issues of giving; empirical papers examining factors relevant to the giving decision (see for instance Williams, 2003; Williams and Barrett, 2000 and Edmondson and Carroll, 1999) and finally longitudinal and cross sectional studies (see for instance Campbell, Moore and Metzger, 2002, Brammer and Millington, 2003 and Campbell and Slack, 2006). This study draws upon the first two strands by examining and developing the case for giving and also the role of the employees within any disclosed philanthropy policy. It is these aspects of the literature that are now presented.

The initial focus of some of the earlier research into charitable giving was discussion around the moral and economic issues raised. These studies examined whether companies should be giving to charity at all. The moral and social implications of charitable giving and the role of corporate philanthropy in both business and social policy was explored by, for example, Moore (1995), Campbell, Gulas and Gruca (1999), Pearson (2000) and Dean

(2001). Arguing from an agency perspective (Jensen and Meckling, 1976; Fama, 1980), Friedman (1970) examined the potential moral and economic conflict of companies giving away what he considered to be shareholders' money to charitable causes and that the explicit objective of any company is to maximise profits and in turn maximise shareholder wealth. From a company economic perspective, charitable giving may be acceptable, Friedman argued, if it leads to a direct economic benefit for the company and can thus be viewed in terms of *de facto* business investment. Corporate philanthropy could thus be justified if it served an underlying business objective. Meyerson (2006) cited increased customer loyalty, brand strengthening or improving employee teamwork and motivation as such examples whereby the company is able to harmonise giving with achieving other internal and external business objectives. Dean (2001, 302) found that 'public companies were increasingly anxious to make connections between corporate activity in the community and business activities' and 'were constantly dealing with the management of reputation'. By engaging with local communities through charitable giving companies were more able to facilitate the achievement of wider business objectives. Porter and Kramer (2002) also discussed philanthropy in the context of corporate economic advantage examining how to maximise the social and economic impact of charitable contributions. More recently McCracken (2004) concluded that corporate philanthropy will enhance the corporation's reputation and can advance financial performance. This is consistent with Brammer and Millington and Pavelin's (2006, 241) conclusions that 'philanthropy plays a significant role in influencing the perceptions of external stakeholders'.

In parallel with this general economic body of literature the concept of strategic philanthropy emerged as to how companies could maximise their business objectives aligned to philanthropic expenditures. One of the earliest studies, Haley (1991) examined how managers use corporate giving to influence stakeholder opinion. Post and Waddock (1995) and Saiia, Carroll and Buchholtz (2003, 185) identified strategic philanthropy as being when 'the corporate resources that are given have meaning and impact on the firm as well as the community that receives those resources'. Thorne, Ferrell, O. and Ferrell, L. (2003, 360) viewed strategic philanthropy as being the 'synergistic use of a firm's resources to achieve both organisational and social benefits'. In general, the literature now supports a strategic use of philanthropy to achieve economic aims and by doing so addresses Friedman's early concerns over the corporate giving decision (and also see Brammer, Millington and Pavelin, 2006; Seifert, Morris and Bartkus, 2004 and Saiia, Carroll and Buchholtz 2003 and Saiia, 2001)

Whilst most of the extant literature has focussed on the external economic and reputation benefits of strategic philanthropy, internal employee related benefits also result. Involving employees with philanthropy enhances employee morale and their social relationship with the business contributing to increased employee retention, motivation and recruitment. For instance, Brown, Hellard and Kiholm Smith (2006, 856) found that that, 'managers often justify corporate giving on the basis of its claimed benefits to shareholders. Benefits may arise, for example, from goodwill that is created by corporate involvement with charitable causes, leading to enhanced employee morale'. Similarly, Brammer, Millington and Pavelin (2006) highlighted the use of philanthropy to enhance worker and goodwill, McCracken (2006) as a means of boosting employee motivation. Raman and Zboja (2006) found that where companies made charitable donations, organisational commitment was higher for their employees. In practice, Mitchell (2005) found significant opportunities to enhance employee motivation through philanthropy involvement. Nonprofit World (2007, 32) reported 'a direct correlation between a company's philanthropy and its employees loyalty', and Oxfam (2007) found increased staff morale and motivation aiding retention and recruitment. Finally, The Financial Times (2007) reported that a compelling argument for companies engaging in corporate philanthropy was recruitment and retention and San Diego Business Report, 2007, stated 'philanthropy is a great way for companies to increase employee satisfaction'

In a wider context, Hendry and Pettigrew (1986) identified labour (employees) as a strategic resource for achieving competitive advantage, and that to achieve this then employees need to be involved in, and identify with, the organisation. At a similar strategic level, Guest (1987) called for the fit of HR policies with business strategy to achieve mutuality of such policies aimed at generating employee commitment and motivation. Marchington (2001) argued that involvement contributes to organisational commitment and greater employee identification with the organisation. The general issue of involvement and participation of employees in organisations is widely addressed in the extant literature (see for instance Dundon et al, 2004; Delbridge and Whitfield, 2001; and Marchington and Wilding 1983). As Corporate Social Responsibility has become more strategically important to organisations (Norton 2000) then appropriate philanthropic policies can be adopted using direct employee involvement which may in turn enhance organisational culture. Brammer, Millington and Pavelin (2006) building on Donaldson (2001) examined the concept of centralization; where decision making occurs within an organisation. For charitable giving, organisations have the chance to engage employees in the decision making process, so dispersing the decision making process beyond the senior management layer.

By engaging employees in philanthropy at either a policy making level or through participation in giving, organisations may promote a stronger organisational culture. Bratton and Gold (2007, 442) argued that employees voice and involvement plays a 'critical role in constructing and maintaining a strong organisational culture'. Cox, Zagelmeyer and Marchington (2006, 250) found that 'greater breadth and depth of employee involvement practices are associated with higher levels of organisational commitment'. Thompson and McHugh (2002, 191) recognise corporate culture as a key factor in 'unblocking the commitment and enthusiasm of employees...and to make people feel they are working for something worthwhile', and the promotion of such corporate culture is consistent with earlier studies such as Guest (1987).

Theoretical framework and hypotheses development

Companies face increasing pressure for greater transparency and accountability, in part arising from recent corporate failures (Enron, Worldcom, Northern Rock) and accordingly this research examines the policy disclosure to stakeholders, informing them of charitable donations. By combining employee policy involvement and transparency of disclosure, this research draws upon both agency and stakeholder theories. Whilst agency theory is normally associated with a shareholder wealth maximisation objective, this unduly restricts the concept of agency to management and shareholders. By adopting a wider perspective agency costs are also reflected in the potentially asymmetric relations between managers and employees. At both shareholder and employee levels an accountability relationship exists between agents (directors and managers) and principals (shareholders and employees respectively) for all material decisions to be communicated and transparently accounted for.

Harrison, Bosse and Phillips (2007) recognise the need for organisations to attend to the needs of a broad group of stakeholders to maximise competitive advantage, rather than just a focus on shareholders. Similarly, Shankman (2006) contends that agency theory must include recognition of all stakeholders and is consistent with Jensen's (2002) proposition of enlightened value maximisation which accepts the maximisation of the long run value of the firm and the trade off amongst its stakeholders. Donaldson and Preston (1995, 68) summarise that there is no 'prima facie priority of one set of interests and benefits over another', and that stakeholder interests are both internal (for example employees) as well as external (for example shareholders and customers). Employees are a critical internal stakeholder and necessary to achieve competitive advantage, in keeping with shareholder wealth maximisation, facilitated through employee commitment, promotion of corporate culture and identity. This study uses agency theory to explain the need for disclosure of charitable giving and associated policies to shareholders (and other stakeholders) and through stakeholder theory examines the need for employees to be involved in both policy decision making and the associated charitable giving of the organisation.

Issues surrounding the involvement with policy and subsequent conveyance of information to stakeholders (including shareholders) underpin the research questions in this paper. Relevant disclosure in the annual report, as a key reporting document, provides clear communication to stakeholders and may facilitate increased trust and confidence. Whilst financial results, levels of staffing, governance are procedurally prescribed under the various financial reporting standards and codes of governance, no such standard exists for the management or disbursement of charitable donations. The mandatory reporting of charitable donations is limited (see Cowton,1989 for a discussion of issues relating to disclosure requirements in this area) and are set out in Section 19, Companies Act (1967) and updated Schedule 7, Companies Act (1985) as follows: 'Political and Charitable Gifts'. "If the money given exceeded £200 in amount there shall be contained in the Directors' Report for the year, the purposes and amount of money given." This requirement does not cover donations made in kind and in non-cash terms.

Although the statutory disclosure requirement is limited, in view of the monetary amounts involved, transparency, associated reduction in agency costs and wider accountability to stakeholders, it would follow that companies will have clear policies that outline their general policies towards such giving. Such policy disclosure would help discharge their accountability to all stakeholders and may cover for instance, policy formation, targeted recipient groups or monetary levels.

- Hypotheses 1: All companies will disclose charitable giving policies in their annual reports

The literature has shown employees as a key stakeholder group and the potential economic and organisational benefits of involving them with corporate giving. This may contribute to enhanced morale, recruitment and retention strategies and the facilitation of organisational culture and identity. To optimise the level of employee involvement with corporate philanthropy hypothesis 2 is as follows:

- Hypothesis 2: All companies disclosing charitable giving policies will involve employees in policy making and charitable giving decisions

Hypothesis 2 is potentially limited to only those companies with a philanthropy policy which may not capture the full sample of companies included in the study. In order to reflect the general level of employee involvement at both a company wide level and more specifically with philanthropy a further two hypotheses are advanced. Hypothesis 3 relates to the specific involvement, and reporting, of employees by companies in philanthropic activities, either through narrative or pictorial representations. Hypothesis 3 is as follows:

- Hypothesis 3: All companies will report employee involvement in corporate philanthropy activities

Hypothesis 4 is proposed to capture the reporting of general involvement of employees in companies, and to help identify any relationship between general involvement and philanthropy policy involvement

- Hypothesis 4: All companies will report employee involvement within the organisation

Each of the four hypotheses will be considered respectively in the discussion following the presentation of the research findings.

Research methods

To address the posed hypotheses and to examine the overall research question of philanthropy policy, reporting and employee involvement, a research instrument was devised involving the capture of charitable donations disclosures from the annual reports of all companies in the FTSE 100[2] (sorted by market value as at 24 February 2008[3]). The FTSE 100 was used to reflect a sector wide sample and as all companies within the sample are international in their operations, employing around 4.7 million people worldwide, and so some evidence of employee involvement with philanthropy and policy can be gained on an international, rather than just UK, perspective. Additionally, with increased levels of employee and other voluntary disclosure content, examples of best practice may be identified.

The annual reports were downloaded from the companies' websites in .pdf format. In order to ensure that all relevant disclosure was captured, the search facility in Adobe Acrobat reader was employed using the words 'charit' and 'philant'. This enabled all relevant narrative to be identified containing the words, 'charity', 'charitable' or 'charities' and 'philanthropy' and 'philanthropic'. Additionally to capture the general level of employee involvement within company reporting a second search was conducted using the terms 'involvement' and 'participation' drawn from Bratton and Gold (2007) Cox, Zagelmeyer and Marchington (2006) and Cabrera, Ortega and Cabrera (2003). These two words were considered rather than just a single word to take into account the disparity of company reporting and the potential ambiguity of involvement and participation and reflect the general recognition of the level of general employee involvement. In all cases, the report ending in the financial year to 2006 was used. The content analysis for this study was undertaken in February and March 2008 (the year ended 2007 was not used as not all companies had reported their 2007 results by that time). All data collected was input into Excel and statistical

[2] Large companies only (i.e. FTSE 100) were selected for the study. Size effects in disclosure have been noted by several previous studies (Guthrie and Parker, 1990; Hackston and Milne, 1996; Adams, Hill and Roberts, 1998) suggesting that smaller companies with less exposure will have less reason to report on voluntary issues.
[3] Three companies did not have full pdf annual report documents, or were not listed for 2006 annual reporting. Accordingly the final useable sample was restricted to 97 companies.

correlations calculated using SPSS. The data used a present/not present coding for all search terms. In order to interrogate the contents of the disclosures, a disclosure index was set up on the spreadsheet. Using a ‘record when seen’ method, seven typical content items were captured from the policy disclosures including staff choice. Two additional terms reflected other employee involvement with philanthropy; staff volunteering and matched staff giving. Because any volumetric analysis of such policy disclosures would have yielded very small numbers (see later), a present/not present frequency-based instrument was used to capture meaning by item. This was capable of recording the incidence of disclosure items in the sample as a whole. All philanthropy reporting was copied into Word for further analysis and examples of philanthropy policy drivers and general employee involvement. All findings are presented in the next section of the paper.

Annual reports were used as the reporting document in this study for two reasons. First, from an agency perspective, as the statutory communication with shareholders and a permanent record, the annual report offers management the opportunity to convey any policies the company may have on charitable engagement. By examining annual report disclosures, therefore, the reporting of charitable donations disclosures and employee involvement can be established and by the use of a suitable content analysis instrument, the extent to which corporate charitable donations activity is policy-driven, including employee input, can be explored. Second, the relevant Companies Act (1985) stipulates the location of the compulsory disclosure as the Directors’ Report (Schedule 7, part 1: Political and Charitable gifts, clause 2). It would be a reasonable assumption that any communication intended to explain or elucidate the charitable donations would be associated with the mandatory disclosure.

Previous studies have questioned the value of using the annual report for content analysis when examining disclosure topics which many companies report upon in more detail elsewhere (Unerman, 2000; Campbell, Craven and Shrives, 2003). However, the annual report provides a permanent record of company reporting as opposed to web-based ad hoc reports by companies that may change over time or disappear entirely. The relative importance of the annual report is recognised by Beattie and Pratt (2002, 1) who commented that ‘the importance of narrative reporting in annual reports has significantly increased’ and Clatworthy and Jones (2001, 311) who similarly concluded that ‘narratives are becoming increasingly important in external financial reporting’. Furthermore, as the annual report is a mandatory reporting document it enables consistency of research method and control between all companies in the sample.

Findings

General observations

All but three companies in the FTSE 100 made some charitable donations in the year to 2007. Where reporting was in US dollars then all values were translated into £ to ensure consistency of findings across the sample. Given the disparity of market values from across the FTSE100 both absolute amounts of giving and a relative measure of giving were recorded. The relative measure is termed the generosity ratio and records the absolute amount of giving divided by the profit before taxation in the relevant year. This enables greater comparison across all companies in the sample, rather than the finding that large companies give more to charity compared to smaller companies (Adams and Hardwick 1998). In total £362 million was specifically donated to charitable causes, with an average generosity rate of 0.23% of pre tax profits. Two companies reported pre tax losses and for those companies the generosity ration is excluded from the calculations. There is no material overall affect of this on the reported statistics.

All companies making donations provided the mandatory disclosure concerning charitable giving. This was added to, in all but a very small minority of cases (four companies), by additional reporting covering either, or both, philanthropy policy or general narrative and pictorial representation. Companies adopted a wide variety of reporting, ranging from brief policy statements through to very detailed accounts of all of their charitable activities. Similarly with general employee involvement and participation, wide reporting deviations were observed.

Charitable donations and policy reporting

Descriptive statistics detailing company size by market value (MV), total giving, levels of profit before taxation (PBT), generosity percentage and total word count relating to charitable donations disclosures are shown in Table 1 below. This helps to contextualise the overall financial impact of giving with a mean donations value of £3.7 million and a mean number of employees of c.48000 across the FTSE100 companies.

Table 1: Descriptive Statistics for charitable giving FTSE companies 2006

	N	Range	Minimum	Maximum		
	Statistic	Statistic	Statistic	Statistic	Mean	Std. Deviation
MV £m	100	101353	2120	103473	13810.76	19043.104
Giving £,000	97	40900	0	40900	3735.22	7573.561
PBT £'m	97	37167	-14853	22314	1628.28	3769.736
Generosity	95	18	0	18	.229	1.953
Total words	97	1625	0	1625	228.21	239.972
Employees	97	439919	209	440128	48733.38	73338.549

Statistically significant correlations at the 1% level were observed between charitable giving and market value and charitable giving and profit before tax. A full correlations matrix is shown in Table 6 at the end of the paper. These findings are consistent with the prior literature, notably Adams and Hardwick (1998) and Brammer and Millington (2004b). The level of giving was also positively correlated with the number of employees at the 5% level, but as the number of employees is a function of market value and profits (statistically significant at the 1% level) this correlation is not surprising.

The coding differentiated between policy and general charitable donations narrative. Whilst the mean number of words was 228, the majority of this is reflected in general narrative reporting, with the most exceptional result of 1625 words provided by Old Mutual. As policy reporting is more succinct, examples of which are shown in Table 3 below, policy disclosure, and categories of policy driver, are presented on a frequency, rather than word volumetric, basis.

Table 2: Corporate philanthropy policy disclosure and main policy drivers

Content of disclosure (n = 97)	Number of companies disclosing	Number as a percentage of number disclosing policy
Companies with UK disclosed charitable giving	94	N/A
Philanthropy policy	74	N/A
Local community projects	43	58%
Priority area for giving specified	42	57%
Support core business activities	28	38%
Size of giving	12	16%
Employees in policy	46	62%
comprising the following sub-groups		
Staff choice	20	27%
Matched funding	27	37%
Volunteering	27	37%

Of the 94 companies making charitable donations, the majority do also disclose some element of philanthropy policy, with most policies including a number of the policy areas shown. Conversely it is true that 20 of the companies making donations chose not to disclose any policy. The main policy drivers are local community involvement, specified priority areas of the business and employee involvement. The latter is split between three areas of direct staff choice, perhaps the most pertinent policy aspect but with the least frequency, matched funding and volunteering. Nevertheless 62% of companies that disclose philanthropy policy do include an employee aspect as part of that policy. The correlation of companies disclosing a philanthropy policy and the inclusion of employees in the policy was statistically significant at the 1% level. With regard to matched funding this was correlated at the 1% significance level with the reporting of philanthropy policy and also the inclusion of employees in policy making. By adopting a matched funds approach companies are able to combine employee contributions, employee involvement and their own charitable commitment.

There are two other common drivers that influence philanthropy policy. Firstly, many policies refer to support of local projects, or helping local communities in which we operate. Secondly, priority areas and policies highlighting this aspect will name specific target areas that may, or may not be, in line with their core business, but instead may be more used to enhance reputation and impression management such as donations to health and education charities.

Typical examples of policy disclosure by the main categories are shown in table 3 below.[4]

Table 3: Policy disclosure examples

Content of disclosure	**Example of disclosure**
Local community projects	Alliance and Leicester: In 2006, we continued to support local charities and community activities Prudential: Prudential is committed to supporting the communities where it is an employer
Priority area	Bunzl: support a cross section of projects within registered charities in the fields of healthcare, education and disability Rolls Royce: Our policy is to give priority to activities supporting education, the environment, arts and culture, and economic and social regeneration
Core business activities	Royal Bank of Scotland (RBS): Our priorities in 2006 were promoting financial inclusion and capability Smith and Nephew: The Group's principles for charitable giving are based on criteria relevant to its business, with priority given to medical education
Staff choice	Aviva: Muscular Dystrophy, which was chosen by employees in the United Kingdom as their "charity of the year" British Energy: This year our staff chose Help the Hospices, the national charity for the hospice movement, as the British Energy Charity of the Year for 2006/07 Capita: a 3rd charity voted for annually by employees –which was Cancer Research UK in 2006 Lloyds TSB: The Charity of the Year is chosen in an open ballot of staff

[4] All quotes are verbatim from 2006 annual reports. This applies to tables 3-5.

	HBOS: A special television programme in January 2007 featured the short-listed charities for HBOS's charity of the year, for which HBOS colleagues then voted electronically and by telephone.
Matched funding	3i's charitable policy aims to support: charitable activities of staff. 3i matches donations made by UK staff under the Give As You Earn scheme ("GAYE") and the proceeds of staff fundraising efforts Aviva The Company allocates a part of its budget to matching contributions raised by staff
Volunteering	British Gas: The Group donates staff time to organised volunteering schemes, and operates a Group-wide matched funding scheme for employees who raise money for charity Prudential: In December 2005, The Chairman's Award, the Group's international employee volunteering programme was launched across the Group Reuters: All employees may take one day of company time each year to engage in community activities

Away from policy reporting, all companies (except four) that made donations also disclosed additional descriptive narrative. This covered their charitable activities and the general involvement of employees in such activities and also included pictorial representation of staff engaged in charitable work. The total number of words reported by companies in relation to charitable giving was positively correlated at the 1% level with philanthropy policy reporting and also with the inclusion of employees in policy. It may be that companies with clear policy are more able to disclose a higher level of information regarding charitable donations.

Typical examples of such general philanthropy reporting and the involvement of employees are shown in table 4 below:

Table 4: Charitable donations narrative disclosure

Rolls Royce: In 2006, examples included: – a series of team challenges which involved 160 senior managers completing community projects in Berlin during the annual Senior Management Conference; – providing business mentors and advisers through The Prince's Trust, Young Enterprise and Arts & Business; Next: Following the Indian Ocean tsunami in December 2004, the Group established a charitable trust to co-ordinate the distribution of over £790,000 of funds raised and donated

by the Group and its directors, employees, associated companies and suppliers. The construction of a 146 home village in Sri Lanka with central social facilities is now almost completed, with 120 houses now occupied by displaced families.

Reuters: In 2006, over 3,000 employees from 58 locations participated, sharing their skills on projects ranging from hosted school visits, training workshops for community groups and fundraising work. Reuters volunteers also continued to work on house building projects run by Habitat for Humanity. In the twelve months to March 2007 volunteers worked on projects in Sri Lanka, India, New Orleans, and South Africa.

London Stock Exchange: One of the highlights of the programme this year was when we divided the company into 10 teams and challenged each to raise enough money to sponsor an ‘adopted’ child through a Brainwave programme for a year. The staff response was magnificent, and the £40,000 raised through this initiative exceeded our target figure by 30 per cent.

Home Retail Group: GUS takes an active role in community activities, supporting charities and working directly with local projects:_ Taking part in these activities is popular with our staff – they feel that they are contributing to their communities and that the Company is supporting them in this. They are also able to learn new skills when working together

In addition to examining specific employee involvement within philanthropy the annual reports were also interrogated for more general involvement and participation of employees within their organisations. In total 45 companies reported on employee involvement and seven companies reported employee participation. Involvement and number of employees was correlated at the 5% significance level. Given the more general use of involvement and also the more decision making relevance of participation the relative levels of reporting are not surprising. However the overall reporting level of employee involvement only accounts for half of the overall sample covered in this study. In general, employee involvement reporting reflects internal communication of information and issues relevant to all employees rather than any direct involvement in policy or decision making and is thus distinct from employee involvement in charitable donation policy content. Examples of employee involvement reporting are shown in Table 5.

Table 5: Employee involvement reporting

Rolls Royce: We continue to work closely with employee representatives to improve the quality of employee engagement and participation in the development of the business

British Airways: An important part of our strategy is to continue our focus on Employee Involvement. The Employee Involvement initiative has created a foundation for developing new ways of communicating, managing and involving our people.

BSkyB: Involvement; The views of Sky people are important and valuable. We have a variety of ways in which we encourage the involvement of our people in helping to shape Sky’s future.

Carphone Warehouse: The Group places significant emphasis on its employees’ involvement in the business at all levels

First Group: The Group is committed to employee involvement and uses a variety of methods to inform, consult and involve its employees in the business. These include subsidiary company newsletters and circulars and also First Edition, a Group-wide newsletter, which is sent to all employees across the Group on a biannual basis.

HSBC: HSBC Holdings continues to regard communication with its employees as a key aspect of its policies. Information is given to employees about employment matters and about the financial and economic factors affecting HSBC's performance.

Discussion and conclusions

This paper has investigated FTSE100 company disclosure of philanthropy policies and general narrative charitable reporting and more specifically the inclusion of employees in those disclosures. Additionally it has also examined the general level of employee involvement in company reporting. The findings highlight a disparity of company reporting at both a policy disclosure level and also concerning employee involvement in formulating charitable donations policy, despite the claimed benefits of employee motivation and retention that arise from employee involvement with charitable giving (Brown, Hellard and Kiholm Smith, 2006, McCracken 2006, Ramon and Zjoba, 2006). Companies have the opportunity with corporate philanthropy to actively engage employees with both charitable activities and also to include them within policy making. The findings show that whilst some companies do involve employees in their philanthropy policy other companies disclosing policy adopt a more centralised approach, not including employees. This is missed opportunity as philanthropy serves a dual role of enhancing external reputation and impression combined with an internal role of employee engagement and the fostering of employee commitment and morale. Recent practice based research (McKinsey Quarterly, 2007 and Oxfam, 2007) both concluded on the importance of corporate philanthropy from both an internal (employee) and external stakeholder perspective.

Whilst the benefits of stakeholder engagement and management are recognised through charitable activities, an additional accountability exists for companies giving money away that could be otherwise expended. Accountability is discharged through full reporting and disclosure and would be optimised through clear policy and subsequent narrative description of charitable activities. By providing such disclosures the company is able to demonstrate to all stakeholders its commitment to charitable activities, and the associated benefits, and reduce any agency costs that may arise from non-disclosure.

The findings have shown that 94 companies in the study made charitable donations, and all those companies did provide the mandatory disclosure. Given the need to make such disclosure, the general stakeholder benefits associated with philanthropic activities and the increased level of governance in reporting, it was expected that all companies would provide some policy statement regarding charitable disbursements. 74 of the 94 companies disclosed charitable giving policies in their annual report. Based upon this, hypothesis 1 is rejected, with 20 companies failing to provide any policy disclosure. Potentially there exists an agency problem over philanthropic policy reporting as there is no clear accountability of giving decisions and subsequent charitable activities where no clear policy is communicated to shareholders. As companies are becoming more strategic in their charitable giving (Brammer, Millington and Pavelin 2006, Saiia, Carroll and Buchholtz 2003) disclosures aligning philanthropy to business needs would discharge this problem. Similarly if companies wish to enhance employee involvement with charitable activities then a clear signal through policy would facilitate this.

Employees were included in philanthropy policy disclosure by 46 companies and were correlated at the 1% significance level with policy disclosure and overall philanthropy reporting content. Employees are a key stakeholder group and their involvement with policy may facilitate increased morale, commitment and so contribute to enhancing corporate ethos and culture (Meyerson, 2006; Brammer Millington and Pavelin 2006). Employee involvement in policy comprises three potential areas of inclusion, staff choice, matched funds and volunteering. All three provide employees with clear engagement in the company's charitable activities, although staff choice of charity is arguably the most powerful although only 20 companies included this within their reported policy. 28 companies that provided policy disclosure did not include any aspect of employee involvement in policy and accordingly hypothesis 2 is also rejected. Whilst 46 companies have included employees it is perhaps a missed opportunity for other companies, who by having a policy and not including employees are not maximising the internal benefits of philanthropy. If we are to apply Brown, Hellard and Kiholm Smith's (2006, 867) general finding that 'philanthropic objective is to enhance firm image and employee morale' then clear evidence of employee involvement in philanthropy should be forthcoming. At a high level this would by being involved in policy setting, at a lower level in the discharge of the firms philanthropic giving.

The general (non-policy aspect) reporting of philanthropy and employee involvement was also examined. Only a very small minority of companies (four) failed to disclose additional narrative information on their charitable activities beyond the statutory disclosure requirement. All other companies provided narrative detail of this and included detail of employees in such activities. Both narrative reporting and pictorial images of staff involvement were employed. Whilst this recognises staff it is also conceivable that such reporting is used to convey messages of happy staff and a committed and cared for workforce and forms part of overall impression management. To alleviate such concerns employees should be part of policy setting as well as general reporting narrative, so moving from a passive to active role in their engagement with philanthropy. Not all companies provide narrative about either their charitable activities, or about any role that the employees play in such activities and accordingly hypothesis 3 is rejected. Given the growth of annual reports over the last decade it is surprising that philanthropy activities, given their good news orientation, is not reported across all of the companies in the study.

Involvement of employees in philanthropy policy rather than philanthropic activities, may be indicative of the general level of involvement of employees in companies. The final part of this study examined the general level of employee involvement reporting. Again the level of reporting was mixed across the companies in the study, with some providing detailed disclosure of involvement and communication practices to engage employees with the organisation. In common with the disparity of philanthropy reporting hypothesis 4 is rejected as only 52 companies in the study provided such disclosure.

Employee involvement at an organisation wide level is viewed as a key factor in corporate culture and promoting competitive advantage. Philanthropic activities provide companies the opportunity for good news reporting and also to fully involve employees with both charitable activities and policy setting. This serves to enhance internal stakeholder involvement and commitment. By policy setting and providing appropriate disclosure the company benefits through enhanced reputation, internal and external, while at the same time answering any accountability and agency concerns.

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Table 6: Correlations for FTSE100 charitable giving and employee involvement 2006

		MV £m	Giving £,000	PBT £'m	Philanthropy policy 1/0	Employees in policy 1/0	Matched staff funds 1/0	Total words	Involvement	Participation	Employees
MV £m	Pearson Correlation	1	.493(**)	.509(**)	-.041	-.144	-.130	-.131	.106	-.004	.346(**)
	Sig. (2-tailed)		.000	.000	.689	.159	.205	.200	.303	.971	.001
	N	100	97	97	97	97	97	97	97	97	97
Giving £,000	Pearson Correlation	.493(**)	1	.066	.163	.089	-.011	.118	.041	-.032	.239(*)
	Sig. (2-tailed)	.000		.520	.110	.386	.915	.251	.694	.754	.019
	N	97	97	97	97	97	97	97	97	97	97
PBT £'m	Pearson Correlation	.509(**)	.066	1	-.138	-.041	-.043	-.047	.015	-.001	.277(**)
	Sig. (2-tailed)	.000	.520		.177	.692	.673	.651	.881	.988	.006
	N	97	97	97	97	97	97	97	97	97	97
Philanthropy policy 1/0	Pearson Correlation	-.041	.163	-.138	1	.459(**)	.364(**)	.400(**)	.130	.155	-.122
	Sig. (2-tailed)	.689	.110	.177		.000	.000	.000	.205	.128	.234
	N	97	97	97	97	97	97	97	97	97	97
Employees in policy 1/0	Pearson Correlation	-.144	.089	-.041	.459(**)	1	.536(**)	.532(**)	.066	.226(*)	-.051
	Sig. (2-tailed)	.159	.386	.692	.000		.000	.000	.521	.026	.622
	N	97	97	97	97	97	97	97	97	97	97
Matched staff funds 1/0	Pearson Correlation	-.130	-.011	-.043	.364(**)	.536(**)	1	.496(**)	.025	.340(**)	-.046
	Sig. (2-tailed)	.205	.915	.673	.000	.000		.000	.810	.001	.654
	N	97	97	97	97	97	97	97	97	97	97
Total words	Pearson Correlation	-.131	.118	-.047	.400(**)	.532(**)	.496(**)	1	.028	.432(**)	-.122
	Sig. (2-tailed)	.200	.251	.651	.000	.000	.000		.784	.000	.236
	N	97	97	97	97	97	97	97	97	97	97
Involvement	Pearson Correlation	.106	.041	.015	.130	.066	.025	.028	1	.060	.200(*)
	Sig. (2-tailed)	.303	.694	.881	.205	.521	.810	.784		.559	.049
	N	97	97	97	97	97	97	97	97	97	97
Participation	Pearson Correlation	-.004	-.032	-.001	.155	.226(*)	.340(**)	.432(**)	.060	1	.000
	Sig. (2-tailed)	.971	.754	.988	.128	.026	.001	.000	.559		1.000
	N	97	97	97	97	97	97	97	97	97	97
Employees	Pearson Correlation	.346(**)	.239(*)	.277(**)	-.122	-.051	-.046	-.122	.200(*)	.000	1
	Sig. (2-tailed)	.001	.019	.006	.234	.622	.654	.236	.049	1.000	
	N	97	97	97	97	97	97	97	97	97	97

** Correlation is significant at the 0.01 level (2-tailed).
* Correlation is significant at the 0.05 level (2-tailed).

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Corporate "Philanthropy Strategy" and "Strategic Philanthropy"

Some Insights From Voluntary Disclosures in Annual Reports

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To develop this study of strategic philanthropy in the United Kingdom, voluntary charitable donations policy disclosures were captured from the annual reports of two samples of U.K. companies: one of the entire Financial Times Stock Exchange 100 at year-end 2002 and another of 14 selected companies over a 15-year period. Post and Waddock's descriptions of "philanthropy strategy" and "strategic philanthropy" were employed to establish the extent to which these concepts were conveyed to readers of annual reports based on the belief that high disclosure serves both agency accountability to shareholders and the information needs of soliciting charities. Conclusions drawn include that although there is a relatively high level of policy disclosure, the detail of narrative in, and consistency (over time) of, these disclosures is very patchy, and only a minority of companies show evidence of adopting a fully strategic approach to philanthropy.

Keywords: *content analysis; community involvement; charitable; disclosure; philanthropy*

Corporate charitable donations policy or strategy and its reporting have received a limited amount of attention in the academic literature. Studies based on American samples have been published in recent years (Saiia, Carroll, & Buchholtz, 2003; Seifert, Morris, & Bartkus, 2004, for example) but there is less by way of research based on British companies. This study aims to contribute to the corporate philanthropy literature in general and to the understanding of the strategies adopted in respect of charitable donations in particular.

Post and Waddock (1995) drew a helpful distinction between "philanthropy strategy" ("The firm is orderly in the methods and procedures it uses to give money away"; Saiia et al., 2003, p. 185) and "strategic philanthropy" ("The corporate resources that are given have meaning and impact on the firm as well as the community that receives those resources"; Saiia et al., 2003, p. 185). Strategic philanthropy was later described by Thorne, Ferrell, and Ferrell (2003) as being the "synergistic use of a firm's resources to achieve both organisational and social benefits" (Thorne et al., 2003, p. 360). Thus, strategic philanthropy has a dual objective of corporate value added and charitable benevolence. Importantly, strategic philanthropy imputes to donors motives other than altruism in their engagement with charitable involvement (Burlinghame & Young, 1996).

Saiia et al. (2003) found evidence for strategic philanthropy in their survey of U.S.-based companies and appeared to find it widespread (see also Mecson & Tilson, 1987; Smith, 1994). Both concepts (philanthropy strategy and strategic philanthropy), however, have received little attention in British academe. Unlike in the United States, no substantial empirical studies have been performed in the United Kingdom to examine the extent to which policy is in place to guide business philanthropy and to understand the contents of any policies that do exist. Few studies have sought to compare and contrast approaches to corporate giving in the United Kingdom and the United States, but where evidence does exist (D. J. Campbell, Moore, & Metzger, 2002), it suggests that corporate giving against pre-tax profits in the United States is substantially higher than in the United Kingdom.

There is some evidence to support the belief that British companies have at least given some thought to strategy in this area. Moore (1995) examined the policy disclosures of Percent Club[1] member companies in the 1993 Percent Club report and found that many companies had considered the types of causes they wished to support and the broad themes that might, at least in part, inform their philanthropy. How consistent this policy may have been over time and how it may be expressed to shareholders has, however, hitherto been unexplored.

Issues surrounding the conveyance of this information to stakeholders (including and probably predominantly shareholders) underpinned the research questions in this article. In other areas of business policy, disclosure in the annual report is seen as material to investment decisions, and the assumption of transparency in reporting underpins investor confidence. It is a fiduciary duty of company agents to their shareholders to explain all material business decisions as they affect profit and dividends. Although many other areas of resource allocation are procedurally prescribed in the various financial reporting standards, no such standard exists for the management or disbursement of charitable donations and so any related disclosure on the issue is entirely voluntary.[2] The extent to which companies observe this nonmandatory reporting is the subject of this article. An optimal accountability relationship between agents and principals would exist when all costs were transparently accounted for. Where the costs are potentially material to dividend and social performance, the need for this accounting is maximized. Hence, although not mandatory, "good" accounting would observe a high level and detail of voluntary disclosure in this area. Being the statutory communication with shareholders, the corporate annual report would, ex ante, be the most appropriate vehicle for such disclosures.

From an agency perspective, the disclosure of policy and reassurances to shareholders that such policy is unambiguously strategic would be expected in good accounting. Corporate governance and reporting "failures" (BCCI, Maxwell, Enron, WorldCom, etc.) are among the factors that have given rise to shareholder pressures for greater clarity and consistency of reporting. Discretionary disbursements, such as charitable donations, are an area of potential resource misappropriation, hence the need for greater clarity in their accounting.

In this study, annual reports were analyzed for the extent to which they contained narrative describing both philanthropy strategy and expressions of strategic philanthropy. The study employed a disclosure index to resolve meaning from voluntary disclosures. Based on two samples—the U.K. Financial Times Stock Exchange (FTSE) 100 at year end 2002 and a sample of 14 companies studied over a 15-year period (to explore the historical context of these disclosures)—the study was able to test for the different ways in which firms approached the reporting of philanthropy, the extent to which strategic philanthropy was conveyed, and the consistency of philanthropy strategy disclosure both cross-sectionally in 2002 and longitudinally over the 15-year period.

The rest of this article proceeds as follows: In the next section, the literature on charitable donations in general and charitable donations policy in particular is reviewed. The sample and method are then discussed. Finally, the findings are presented and conclusions are drawn.

Background and Literature Review

Charitable Donations and Voluntary Disclosure

The literature on charitable donations can be broadly considered to comprise a subset of the more general literature on corporate social reporting and performance (Balabanis, Phillips, & Lyall, 1998; Moore, 2001; Moore

Table 1
Summary of Literature in Corporate Charitable Donations by Research Type

Type of Research	Examples
Moral and economic issues raised by corporate charitable involvement	Friedman (1970) Nesteruk (1989) Shaw and Post (1993) Moore (1995) Himmelstein (1997) L. Campbell, Gulas, and Gruca (1999) Pearson (2000) Dean (2001) Porter and Kramer (2002)
Corporate issues and associations between charitable donations and company characteristics	Cowton (1987) Wang and Coffey (1992) M. Adams and Hardwick (1998) Edmondson and Carroll (1999) Williams and Barrett (2000) Brammer and Millington (2003) Saiia, Carroll, and Buchholtz (2003) Williams (2003) Seifert, Morris, and Bartkus (2003, 2004)
Empirical studies; longitudinal and cross-sectional patterns in charitable giving.	Arulampalam and Stoneman (1995) Weeden (1998) D. J. Campbell, Moore, and Metzger (2002) Brammer and Millington (2003)

& Robson, 2002; Preston & O'Bannon, 1997). Among those articles that have specifically explored aspects of charitable donations activity, three main research themes can be identified. These are shown in Table 1.

Although charitable donations from U.K. companies remain small as a proportion of corporate profits (typically less than 0.5% of pretax profits; D. J. Campbell et al., 2002), the actual value of corporate cash donation adds up to a substantial amount. Moore (1995) reported in 1993 that a survey of 1,430 companies in the United Kingdom had collectively donated £169 million in that year. As a part of the research for this present study, the authors calculated that cash donations to U.K. causes from the FTSE 100 companies alone totaled more than £800 million at year ended 2002.[3] From an agency perspective (see, for instance, Jensen & Meckling, 1976, and

Fama, 1980), this figure is attributable to shareholders, and an accounting capable of describing policy with regard to its disbursement would not be an unrealistic shareholder expectation.

It is perhaps curious, then, that so little is required of companies by way of reporting in this area. The only mandatory disclosure under U.K. company law remains the clause first introduced in the 1967 Companies Act (and retained in all subsequent revisions; see Cowton, 1989) to disclose the actual amount in cash given away in each accounting period.[4] All other narrative describing policy or practice in the area of charitable activity is entirely voluntary.

Policy disclosure is of potential import to several audiences. Charitable donations policy disclosure could, for example, assist in accounting for costs and ensuring that any donations are directed so as to support shareholders' long-term interests. For other potential audiences, such as lobby and special interest groups (D. J. Campbell, 2004; Tilt, 1994), such policy may serve as a basis of solicitations or other engagement. It is curious, despite the ostensibly benevolent nature of charitable donations, that so little by way of accounting is required of business organizations. The lack of a requirement to disclose policy effectively leaves all decision making to agents, and it is thus possible for agents (directors) to pursue their own private interests in this matter with no requirement to explain themselves to any other constituency. These may in some cases be at variance with the ethical positions held by shareholders and other legitimate stakeholders, but the lack of a disclosure requirement means that such discordances would not necessarily become known to the stakeholders. The argument for corporate reporting transparency thus suggests that full policy disclosure is inherently desirable—those disclosing charitable donations policy are making a more complete reporting than those not so doing. Furthermore, those companies that not only disclose policy but also provide reassurances to shareholders that all charitable donations serve strategic ends are making optimal accounting disclosures in this area.

Why Should Philanthropy Be Strategic?

Saiia's (2001) thoughtful article subtitled "Strategic Philanthropy Is Good Corporate Citizenship" made the point that

> when a corporation engages in philanthropy it is confronted with the task of allocating corporate resources for activities that are not directly related to its immediate business objectives and thus must consider what is important enough for the corporation to support as an institution within the community. (p. 58)

Given such discretion, each individual giving decision represents an expression of the strategy of the firm in the same way as would be the case for any other resource allocation. Where resource allocations are made subject to assessment of financial return, the efficiency of each allocation is maximized. This model can be applied to charitable donations in the same way as for any other area of resource allocation (such as staff training, for example).

One of Saiia's (2001) conclusions was that "strategic philanthropy increases the level of scrutiny and review of projects that compete for corporate funding" (p. 68). When a return is expected from each giving decision, the utility of each will be scrutinized in a way that would not be the case following a more arbitrary distribution of resources. This, in turn, will provide reward for, and secure ongoing donations to, those charitable causes most able to demonstrate their commensurability with a business's core activities.

It thus follows that maximum net benefit from a company's charitable donations will be obtained when each donation is reviewed from the point of view of its potential contribution to other measures of strategic success. Donations over time are likely to be lower in value terms, more sporadic, and of less consequent use to recipients when they are dripped out inconsistently and at the whim of whoever is distributing funds in a given year. When, conversely, donations are made to causes directly aligned to core business activities and where the motive for giving is therefore not entirely altruistic, those charities that do benefit are more likely to be able to rely more on funding and hence plan more effectively than those for whom the corporate motive in giving is more altruistic.

From an agency perspective, therefore, the case for strategic philanthropy is very strong. Insofar that shareholders may legitimately expect all resource allocations to attract a measurable return, the company's economic responsibility is to seek causes capable of supporting the company's strategy, make donations as appropriate to them on an ongoing basis, and then report this information to shareholders in detailed disclosure and on a regular basis.

Content Analysis

Studies in other areas of voluntary disclosure have employed content analysis methods for the interrogation of corporate communications. Usually comprising two separate analytical stages (coding and measurement), such studies have explored a number of types of voluntary disclosures, most often in annual reports. These have included disclosure on environmental issues (D. J. Campbell, 2003; Deegan & Rankin, 1996;

Patten, 1995), equal opportunities (C. A. Adams, Coutts, & Harte, 1995), general social issues (D. J. Campbell, 2000), accounting ratios (Watson, Shrives, & Marston, 2002), and ethnic minorities (C. A. Adams & McPhail, 2004). The purpose of all content analysis is to infer meaning from content, and this is usually done by representing narrative intent using numerical data. The numerical data can then be analyzed to gain an understanding of the content in a manner than enables current and historical comparison of the narrative to be made.

Whereas coding decisions concern rules for identifying different types of disclosure from a general narrative (usually by means of the imposition of consistently applied disambiguation rules), measurement requires content analysts to select an appropriate way of extracting meaning from coded content. Two broad approaches have been prominent. First, semiotic studies—those in which reporting intent is inferred from a proxy in most cases related to volume or frequency of disclosure—have included measurement by word count (D. J. Campbell, 2003, 2004; Deegan & Gordon, 1996; Deegan & Rankin, 1996; Wilmshurst & Frost, 2000), sentence count (Deegan, Rankin, & Voght, 2000; Milne & Adler, 1999), summed page proportions (D. J. Campbell, 2000; Gray, Kouhy, & Lavers, 1995; Guthrie & Parker, 1990), frequency of disclosure (Cowen, Ferreri, & Parker, 1987; Ness & Mirza, 1991), and "high/low" disclosure (Patten, 1991). Second, disclosure index studies have been used in other studies to capture meaning by recording the content of a disclosure by entering data as appropriate into an index comprising pre-agreed disclosure categories (Cormier & Gordon, 2001; Gray et al., 1995; Wiseman 1982). This latter approach is more appropriate when a qualitative assessment is required, such as when the number of items mentioned in a narrative is an important indicator of the comprehensiveness of a narrative or when, as is the case with this study, the aim of an experiment is to establish what is being reported rather than (as is the case with semiotic studies) how much of, or how often (i.e., how frequently), an item is reported.

The choice of the annual report as the medium for capturing voluntary disclosure in this study rests on its importance as the statutory accounting document, produced regularly and over which the company has effective editorial control. It is capable of demonstrating a company's reporting intent with regard to any issue of relevance to shareholders. For the purposes of ascertaining a company's reporting intent with regard to its charitable policies, the annual report would, on the face of it, be the most appropriate, but probably not the only, medium for content analysis. Insofar as the Companies Act requires that the mandatory disclosure of the amount given to charities be made in the directors' report (an auditor-reviewed section of the annual report), it would be reasonable to assume that companies wishing to make voluntary disclosures on the issue would do so alongside or nearby the mandatory disclosure. This assumption is borne out in practice (see later).

Sample and Method

Sample

This study employed two samples to provide both cross-sectional and longitudinal perspectives on the issues of philanthropy strategy and strategic philanthropy. The cross-sectional element was intended to examine how widespread the two practices were in evidence in a given year, and the longitudinal sample was intended to show how they may have changed over time and was partly informed by Seifert et al.'s (2004) comment, when discussing the limitations of their own findings, that "much could be learned from longitudinal data" (p.153).

Insofar that the study set out in part to examine practice in the United Kingdom, only British listed companies were selected for analysis. Previous voluntary disclosure studies have found size effects relating to a number of different types of voluntary disclosure (C. A. Adams, Hill, & Roberts, 1998; Belkaoui & Karpik, 1989; Cowen et al., 1987; Trotman & Bradley, 1981), and accordingly, only large or "relatively large" companies were considered.

For the cross-sectional analysis, the entire population of the FTSE 100 stock market listing was selected as ranked by market value in September 2003. To examine practice in a single period of time, all content analysis was carried out on annual reports for the year ended 2002. This was the last complete year-end for which all FTSE 100 companies' annual reports were available at the time during which the content analysis was undertaken.

The longitudinal sample—that element capable of describing trend—comprised a sample of 14 companies selected from a derived listing of the FTSE 100 members that had been continuous members of the FTSE 100 since January 1988 and that had not undergone any major change (by way of merger or demerger) that may have radically changed the management over that period (so as to control, as far as possible, for radical management change being a factor in changing policy disclosure). A second consideration when selecting the sample was to draw widely from the sectors in the FTSE 100 so as not to have any single sector overrepresented that may subsequently skew the findings. The start date of 1988 was selected on the basis of findings in other areas of voluntary disclosure, particularly those by C. A. Adams & McPhail (2004) and D. J. Campbell (2003, 2004). These previous studies found both frequency and volume of voluntary disclosures to have substantially increased around 1990. By commencing at 1988, this present study was able to sample just prior to this expected general increase in voluntary disclosure (the increase in voluntary disclosure around 1990 was, incidentally, also observed in this study as shown in Table 5). The longitudinal period of 1988 to 2003 produced a longitudinal period of 15 years, which was sufficient to enable statistically valid longitudinal statistics to be calculated.

The final sample for the longitudinal study was as follows:

Insurance and related: Legal and General
Banking: Royal Bank of Scotland, Standard Chartered
Defense and related: BAE Systems, GKN
Property: Land Securities
Food and Drink: Cadbury Schweppes, Allied Domecq
Retail: Boots
Medical equipment: Smith & Nephew
Engineering: Rolls Royce
Media: Granada
Publishing: Pearson, Reed Elsevier

In both the cross-sectional and longitudinal samples, the content of coded policy disclosures was entered on a disclosure index. An examination of the completed index was capable of demonstrating not only the "popularity" of certain components of policy but also the consistency of disclosed policy over time.

Coding for Philanthropy Strategy and Strategic Philanthropy

Content analysis methods raise a number of issues for researchers seeking to infer meaning from content. Insofar that no method is capable of total reliability, markers and signals are sought from narrative content that can be assumed to convey certain content information (Krippendorff, 1980). In the case of the disclosures sought by this study, it was necessary to describe what would constitute evidence for philanthropy strategy and strategic philanthropy when encountered in a narrative disclosure.

Philanthropy strategy was interpreted as that disclosure describing intent on how the company was currently disbursing, or wished to disburse in the future, its charitable giving. Narrative merely describing past activities or giving was interpreted as descriptive and illustrative and was not coded as policy disclosure. In essence, narrative coded as policy or strategy was that content that was interpreted as being of potential use to shareholders seeking agency accountability with respect to disbursements and/or potential recipients. In some instances, this narrative was readily identifiable as "it is the company's policy to . . .," but on the majority of occasions the narrative had to be isolated from an otherwise undisaggregated narrative on charitable donations that may also have included backward-looking descriptive content.

Coding for *strategic philanthropy* also presented a content analysis challenge. It was necessary to describe the type of content that would signal that charitable donations were, at least in part, intended to support the company's main business strategy. Having examined an initial pilot sample of the policy disclosures, two types of content were taken to signify strategic philanthropy. Content explicitly stating that one of the motivations behind the company's philanthropy was to support the business strategy or that donations would be made in areas related to the company's core business was taken as one such signifier (defined as "core business" in Table 2). The second signifier was evidence from the types of causes (identified as "priority areas" in Table 2) supported. Where these were cited and were in the same general area as the company's main business activities, this was also taken as evidence for strategic philanthropy. A Likert-type scale of 1 to 3 was used to compare the company's core business with the types of priority areas identified (1 meaning *highly similar and capable of interpretation of evidence for strategic philanthropy* and 3 meaning *no obvious similarity and unlikely to represent a strategic approach to philanthropy*).

In both cases, disambiguation rules[5] were applied to coding decisions to ensure the minimization of content analysis errors. All narrative was coded by the two authors, and marginal cases were discussed on an individual basis. The level of intercoder agreement was thus 100%.

Findings

Themes in Policy Disclosures

The themes captured in the policy disclosures were developed as the research progressed and as new themes presented themselves. Moore's (1995) themes were helpful in developing the themes for the current study but were inadequate in describing the totality of content in the policy disclosures in all annual reports analyzed. By the conclusion of the coding process, nine themes had been identified as being present in one or more

Table 2
Descriptions of Signifiers for Strategic Philanthropy and Philanthropy Strategy

Signifier	Description
Strategic philanthropy signifiers	
Priority areas	Those areas of charitable work the company was most concerned with were explicitly mentioned. Typically, broad categories were described, for example, education, health, literacy, and so on.
Core business	Companies disclosing this theme described that charitable donations were, at least in part (and usually predominantly), intended to support causes that operated in the same activities as their main business activity.
Other strategy signifiers	
Local community	Companies appeared to want to convey the message that their charitable donations were focused, at least in part, on the communities in which they operated. In some cases these communities were explicitly "local"—typically those physically surrounding the places of their head office or outlets—and others, more ambiguously, described communities in an international sense.
Trust or foundation	A company-named trust or foundation was used to manage and disburse the company's charitable donations.
Percent Club	Being a member of the Percent Club was a material factor in deciding on the amount given in charitable donations.
Target amount	The company explicitly disclosed that it was seeking to donate up to a target amount or wished to increase its giving year-on-year by or up to a target amount.
Matched funding	A part of the company's giving was through matched funding to other funds raised elsewhere (usually by employees).
Committee	Charitable activity and the charitable donations policy was the responsibility of a named management committee within the company.
Employee initiatives	Employees and their preferred causes are (at least) a part of the process by which the company selects causes to support.

policy disclosures. For the purpose of clarity, Table 2, which describes the contents of each theme, shows those themes that signify strategic philanthropy as distinct from the "other" signifiers of philanthropy strategy.

Table 3
Content of Policy Statements by U.K. Financial Times Stock Exchange 100 Companies in Year Ended 2002

Signifier	Percentage of Those Disclosing Policy	*n*
Strategic philanthropy signifiers		
Priority areas	63.6	42
Core business	18.2	12
Other strategy signifiers		
Local community	66.7	44
Trust or foundation	27.3	18
Percent Club	10.6	7
Target amount	13.6	9
Matched funding	1.5	1
Committee	12.1	8
Employee initiatives	15.1	10

Note: In most cases, policy disclosures contained several entries as recorded in the above table; hence sum of all *n* exceeds 66.

Cross-Sectional Sample: FTSE 100 2002 Annual Reports

All FTSE 100 companies reporting in 2002 were found to comply with the legal minimum requirement to disclose the cash amount donated to charitable causes in the year. Of the 100 companies in the cross-sectional sample, 66 were found to have disclosed some narrative capable of interpretation as policy in respect to philanthropy. These narratives were content analyzed using the disclosure index, and the summary findings are shown in Table 3.

Of the 66 companies disclosing policy, 42 (64%) disclosed one or more priority areas. By matching these against the core business of the company in question, the Likert-type scale was able to indicate the extent to which the purported priority areas could be construed as supportive of strategic philanthropy. Of the 42 that disclosed priority areas, 11 companies supported priority areas highly aligned with their core business (scored at Likert-type scale 1), 15 mentioned priority areas interpreted as partially aligned with core business (Likert-type scale 2), and the remaining 16 appeared to have no material connection between the priority areas mentioned and the core business (Likert-type scale 3). Table 4 lists the detail of the alignments for those scored at Likert-type scale 1.

Of the 11 that demonstrated strong alignment between core business and priority area (Likert-type scale = 1), only 4 also disclosed that core business (one of the content categories on the disclosure matrix; see Table 2) was a

Table 4
Listing of all 11 Likert-Type Scale = 1 Priority Area Disclosures (Those Interpreted as Engaging in Strategic Philanthropy on the Basis of These Disclosures)

Company	Core Business Areas of Company	Priority Areas Mentioned by Company
Amersham	Protein separations, discovery systems, and medical diagnostics	Science and education
AstraZeneca	Drugs, health care	Improving health and quality of life and promoting the value of science among young people
BAE Systems	Defense and aerospace	Science and engineering education in schools and colleges
Bradford & Bingley	Financial services (prominently home mortgages)	Four main areas linked to our business: • Preventing and alleviating the causes of homelessness • Personal finance and numeracy education in schools • Disability access to financial services • Social regeneration through our work with housing associations
BT Group	Telecommunications	Tackling big issues where better communication can make a real difference
Cable & Wireless	Telecommunications	Education and basic communications, access to communications and information technology
GlaxoSmithKline	Drugs, health care	Health and education
Land Securities	Property	Aims to regenerate town and city centers across the United Kingdom, providing benefits for the local community
Prudential	Financial services	Actively promoting lifelong financial learning
Shire Pharmaceuticals	Drugs, health care	Medical foundations
Smith & Nephew	Drugs, health care	Individual research for doctors and nurses; focus solely on nursing research

factor in the giving decision. The other 7, therefore, may have either neglected or declined to state unambiguously that their philanthropy was linked with their core business, notwithstanding the evidence from the

Likert-type scale analysis that it was. The 4 that provided core business disclosure and Likert-type scale 1 scoring were Amersham, Bradford and Bingley, Shire Pharmaceuticals, and Smith & Nephew. One possible interpretation of these findings is that companies express their commitment to strategic philanthropy in different ways. If any one signifier (either Likert-type scale = 1 or core business disclosure) was capable of indicating a strategic approach to philanthropy, then the findings suggest that 19 companies that disclosed policy could have an element of strategic philanthropy in their giving.

Longitudinal Analysis: Overall Disclosure Frequencies

The longitudinal sample comprised 14 companies (listed above) whose annual reports were content analyzed for the period of years 1988 to 2002, inclusive. The overall incidence of disclosure of a policy *at all* in the annual report was 127 out of a possible total of 210 (14 companies multiplied by 15 years). This represents an overall disclosure rate of 60%.

The longitudinality of the sample was helpful in shedding light on how the contents of disclosure changed over time. The key statistics are shown in Table 5.

Table 5 shows a number of trends worthy of comment. Among the sample of 14 companies selected for longitudinal analysis, the frequency of policy disclosures per year rose over the period of the study. Prior to 1993, the incidence of policy disclosure was limited to well less than half of the sample (5 of the 14 in 1988, 4 in 1989, 3 in 1990, 5 in 1991, and 6 in 1992). The year 1993 witnessed a sudden increase to 10 of the 14, and this higher incidence of disclosure remained the case until the end, rising slightly overall in the remaining years to 13 out of 14 in the final year, 2002.

Within the overall upward trend, patterns of themes disclosed showed irregularities with regard to trend, and the small numbers of observations involved (especially toward the beginning of the period where the incidence of policy disclosure was low) make statistical analysis problematic. A more robust treatment of the data, therefore, was undertaken to focus more on the overall frequency of disclosure by theme and on the mean rank of each disclosure theme with respect to the others (Table 6). Over the totality of the longitudinal period, the ranked frequency of mention of themes was as shown in Table 6 (this being a summary of Table 5). This shows the relative "popularity" of each theme, in terms of ranking by year, regardless of company or year, across the 15-year period.

Table 6 indicates that overall, companies during the 15-year period rated "local communities" as the most frequent theme mentioned in the policy

Table 5
Frequency of Themes Mentioned in Charitable Policy Disclosures in Annual Reports by Year

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
n (companies disclosing policy in year)	5	4	3	5	6	10	9	9	9	9	9	12	12	12	13
Percentage of total companies in sample	35.7	28.6	21.4	35.7	42.8	71.4	64.3	64.3	64.3	64.3	64.3	85.7	85.7	85.7	92.8
Related to core business	0	50	67	60	33	30	33	44	33	11	22	25	33	33	38
Community related	40	50	67	60	67	60	55	78	78	78	67	67	75	83	69
Matched funding	0	0	0	0	17	0	0	0	0	22	11	17	17	8	8
Trust or foundation	20	25	33	40	50	40	44	33	22	22	22	25	8	8	8
Committee	0	0	0	0	17	10	11	11	11	11	11	8	8	8	8
Employee initiatives	0	0	0	0	0	0	0	11	11	0	11	0	0	8	8
Target amount	20	25	0	20	17	30	11	11	11	0	0	0	0	0	8
Percent Club	40	75	33	40	17	40	33	11	22	11	11	8	17	8	15
Priority areas	40	50	67	40	33	50	55	33	44	33	44	58	25	33	54

Note: Total companies in sample = 14. Frequency of themes is the percentage of those in disclosed policy in given year rounded to the nearest integer.

Table 6
Mean of Ranked Positions by Year and Overall Frequency of Each Theme in Charitable Donations Policy Disclosure

Theme in Policy Disclosure	Mean Rank	Frequency of Mention in Total (all companies, all years)
1. Community related	1.07	87
2. Priority areas	2	55
3. Related to core business	2.5	41
4. Trust or foundation	3.07	31
5. Percent Club	3.27	27
6. Target amount	3.75	11
7. Matched funding	4	11
8. Committee	4.28	11
9. Employee initiatives	4.4	5

Note: Equal-ranked placings were assigned the same rank in any given year. Overall sample = 210 annual reports (i.e., 14 companies over 15 years); total number of policy disclosures in the sample = 127.

disclosure. This was followed by the disclosure of the main priority areas supported (always with disclosure of those priority areas) and then disclosure that charitable donations policy was intended to be aligned with or to support the company's core business activities. Other themes were consistently ranked lower by frequency of mention.

Longitudinal Consistency

The consistency that sample companies adopted toward charitable donations policy disclosure was analyzed in two ways. First, the extent to which each company reported the same themes whenever policy was disclosed was analyzed. Second, an analysis of the actual priority areas mentioned (not just whether priority areas were mentioned but what they were) was carried out to examine the extent to which companies were consistent in their support for certain causes through the years.

Table 7 shows the frequency of theme mentioned by company (all years). The varying proportions of frequency by company by theme against the overall disclosure frequencies by company (*n*) clearly highlight the inconsistencies of disclosure by theme in most of the companies' disclosure histories. It is not necessary (and it would be unnecessarily tedious) to discuss each company's record in turn—it is evident that the majority of the companies in the sample disclosed a number of different themes throughout the

Table 7
Frequency of Policy Disclosure (*n*) and Frequency of Each Theme Disclosure by Company

Company	*n*	Community	Priority Area	Core Business	Trust	Percent Club	Target	Matched	Committee	Employee
BAE Systems	2	2						1		
Boots	11	10	6	2	8	2				
Reed	8	7	4	5		4		2		2
Land Securities	3			3						
Pearson	13	13	3	8		4	6	7		
Cadbury	11	11			4	9				1
Legal & General	12	5	3	11		4	1	1		1
Standard Chartered	11	11	1				1		1	
Royal Bank of Scotland	11	8	7							
Smith & Nephew	15	5	15		15					
Allied Domecq	4	2	3		4	1				
Rolls Royce	10		10	10					10	
GKN	7	4	1			3	3			
Granada	9	9	2	2						1

period of the study. A consistent approach to policy disclosure would show the frequency of each theme to be equal, or close to equal, to *n* in each case. Although this is the case for some companies for some themes (Standard Chartered and local communities, for example), a great deal of reporting inconsistency appears to be evident.

For other themes, a one-off mention here or there seemed to highlight an apparent fickleness of policy. By way of example, Standard Chartered Bank announced in 1993 that the amount it gave to charity as a proportion of pretax profits would be increased in line with an escalating formula (coded in this study as "target amount"). Its figure of giving in that year amounted to 0.07% of pretax profits. It was the same in the following year (after the escalator was meant to have taken effect). In subsequent years, the giving rate fell by almost half to 0.037% of pretax profits. The escalator was not mentioned again after 1993.

The highlighting of longitudinal consistencies in the priority areas supported over time showed a similar variability across the sample of companies (see Table 8). Rolls Royce and Smith & Nephew showed the most consistency in this regard. Specific areas were mentioned in the majority of years (for Smith & Nephew, it was in every year), which, incidentally, were more or less in support of the two companies' core business activities. Smith & Nephew, a medical equipment company, supported the training of doctors and nurses (who will then go on to be potential buyers of the company's products for their entire professional lifetimes), and Rolls Royce (engineering) consistently supported, inter alia, engineering- and science-related causes (Smith & Nephew was one of the four companies demonstrated by the cross-sectional analysis to have shown evidence of strategic philanthropy). Royal Bank of Scotland mentioned priority areas in 7 of the 11 years in which it disclosed policy, and in each case, similar priorities seemed to be present. Its continued support for disadvantaged and "socially excluded" communities appeared to be a prominent theme.

In contrast to these three, some other members of the sample appeared to show no consistency with regard to priority areas. Granada introduced a discussion of priority areas for the first time in 2001 with a single area mentioned: education. By 2002, the priority area also included arts. Standard Chartered announced priority areas only once in the period of the study. In 1999 it announced that its priority areas were "youth, health, and education." This disclosure was not repeated in subsequent years. Similarly, GKN made only one disclosure on priorities in the period studied. In 1999 only, it announced priority areas of "education and health."

Table 8
Listing of All Priority Areas Mentioned by the Sample of Companies by Year

Company	Year	Priority Areas Mentioned
Boots	1992	Health care, children, young people and homeless (in) areas of high unemployment
	1993	Focus is on Nottingham . . . health care, education, and economic development
	1994	Focus is on Nottingham . . . health care, education, and economic development
	1998	Nottinghamshire: health, economic development, education, and family welfare
	1999	Nottinghamshire: health, economic development, education, and family welfare
	2002	Health, education, and employee volunteering
Reed	1989	Literacy
	1990	Literacy
	1991	Literacy
	2002	Education for disadvantaged young people
Pearson	1995	Education
	1996	Education and young people
	2002	Education in United Kingdom and United States
Legal & General	1993	Medical research, quality of life in retirement, crime prevention, and small business development
	1994	Medical research, quality of life in retirement, crime prevention, and small business development
	1997	Youth, welfare, and health
Standard Chartered	1999	Youth, health, and education
Royal Bank of Scotland	1988	Job creation, national heritage, and environment
	1996	Education, environment and heritage, financial counseling and training, health, and community empowerment
	1998	Education, job creation, social exclusion, and the development of small businesses
	1999	Education, addressing financial exclusion, and microeconomic development
	2000	Social exclusion [only]
	2001	Education, enterprise in disadvantaged communities, and financial education
	2002	Education, enterprise in disadvantaged communities, and employment
Smith & Nephew	1988	Doctors' and nurses' scholarships through the Smith & Nephew Foundation

(continued)

Table 8 (continued)

Company	Year	Priority Areas Mentioned
	1989	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	1990	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	1991	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	1992	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	1993	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	1994	Smith & Nephew Foundation . . . for the funding of research, education, and training in the medical and nursing professions
	1995	Medical and nursing
	1996	It [the foundation] aims to improve clinical practice in medicine, surgery, and nursing
	1997	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	1998	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	1999	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	2000	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	2001	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
	2002	Doctors' and nurses' scholarships through the Smith & Nephew Foundation
Allied Domecq	1993	Education, the arts, and the environment
	1994	Education, the arts, and the environment
	1999	Education, the arts, and the environment
Rolls Royce	1993	Military benevolent associations and engineering, science, and education
	1994	Military benevolent associations and engineering, science, and education
	1995	Military benevolent associations and engineering, science, and education
	1996	Military benevolent associations and engineering, science, and education
	1997	Military benevolent associations and engineering, science, and education
	1998	Military benevolent associations and engineering, science, and education

(continued)

Table 8 (continued)

Company	Year	Priority Areas Mentioned
	1999	Education, engineering, science
	2000	Education, engineering, science
	2001	Education, engineering, science
	2002	Education, engineering, science
GKN	1999	Education and health
Granada	2001	Education
	2002	Arts and Education

Note: Quotations of priority areas are verbatim wherever possible.

Boots was a relatively frequent reporter of priority areas (6 of the 11 years in which policy was disclosed), but it reported a narrowing of its focus in 1993 when it announced that its efforts were thenceforth be concentrated in Nottinghamshire—the area in which its head office had been located since the company began.

Discussion

There are two conceivable ways of establishing the motivations of companies with respect to their strategies for philanthropy: to engage them directly by way of a questionnaire or similar (as Saiia et al., 2003, did) or to interrogate narrative previously disclosed on the subject in question (as this study has done). Both of these approaches have their advantages and limitations. Saiia et al.'s (2003) study suffered from a low useable return rate (15.6%), which in turn limited the extent to which they could generalize and summarize from their findings. In its favor, however, their method allowed the authors to claim that those interlocutors that did complete and return the questionnaire would probably have provided a reliable report of the issues asked about.

This study took a contrasting approach. Using content analysis methods previously employed in other areas of business research, this study interrogated the existing public disclosures made to shareholders in respect to philanthropy. This approach had the advantage of broad sampling (companies were unable to refuse to participate in the exercise) and a historical perspective not available to direct company interrogation. Against these advantages are the issues associated with the use of voluntary disclosures for the inference of intent and meaning: For reasons of negligence, mendacity, or intentional misdirection, companies may not always mean what they say in a given narrative.

Incentives to make accurate and adequate voluntary disclosures (of many types) are present as a consequence of the motivation to minimize agency costs, however. If a narrative disclosure can address a potential or actual shareholder concern at minimal cost, then agents will tend toward high disclosure on a given issue (Camfferman, 1997). In the case of corporate philanthropy, there is no obvious commercial sensitivity to any associated disclosure, and insofar that disclosure of the cash amount is legally required and an opportunity thereby naturally exists to make an associated explanation, it is likely that it is defensible to infer meaning from voluntary narrative disclosure in this area. The article therefore claims that validity can be attached to the conclusions drawn from the foregoing findings.

The questions addressed in this study concerned the extent to which U.K. firms had a strategy at all with respect to philanthropy (philanthropy strategy) and, where strategy was found to exist, whether philanthropy was used by companies as a part of their overall business strategy (strategic philanthropy).

The cross-sectional sample showed that a majority (66%) of U.K. FTSE 100 firms reported their thinking with respect to intent or policy associated with charitable giving. The content analysis instrument resolved policy at the level of the phrase, and so in many cases, such policy intent may have been little more than a vague expression of intent. In others, however, the number of themes disclosed (Tables 2 and 3) suggested that the disclosure may have been triggered by a more detailed consideration of policy issues. The longitudinal study of the 14 selected companies showed a mixed picture. Some were found to have been very consistent in their policies, whereas others showed little evidence of consistent thought on the subject. Others still showed signs of fickleness and apparent indecision. The conclusion can thus be drawn that philanthropy strategy is inconsistently observed both longitudinally and cross-sectionally.

Strategic philanthropy is less in evidence than philanthropy strategy. Although 12 companies made mention that charitable donations were aligned or intended in part to support the core business, and 7 demonstrated that their priority areas mentioned were clearly aligned with the core business, only 4 demonstrated a high level of commitment to strategic philanthropy by disclosing in both categories. Of these 4, 3 were associated with health care products. Notably, it was Smith & Nephew—one of the selected 14 studied longitudinally—that demonstrated the most longitudinally consistent approach to the alignment of priority areas with core business. These findings do not preclude the possibility that health care and medical companies are among the more strategic in their approach to philanthropy. It is not possible to provide clear reasons for this, but it is possible that the presence and public profile of a lot of medical and health charities make finding suitable ("strategic") causes easier for health care companies than for other types of business.

From an agency perspective, it is possible to interpret these conclusions as indicative of a less-than-ideal approach to resource management among FTSE 100 companies in respect to voluntary donations. The findings also support the belief that charities are being ill served by business corporations that, with a few notable exceptions, observe little consistency in funding from year to year. Both charities seeking consistency of support and shareholders seeking reassurances that all discretionary disbursements made are strategically validated would be likely to approve of a more strategic approach to giving. The total largesse of more than £800 million (in year 2002) was, this study is able to conclude, strategically directed by only a small number of companies. A substantial amount of giving was made in such a way as to be unaccountable to shareholders in the manner of its disbursement.

At least two avenues for further research are suggested by this study. First, neither the method employed in this study nor that of Saiia et al. (2003) was able to fully explore the internal management processes and protocols undertaken in the area of corporate philanthropy. An empirical study involving successful engagement with a number of companies willing to describe such processes would represent a worthwhile opportunity for further research. Second, little is known on the sectoral variables that affect changes in corporate approaches to philanthropy. This study has found evidence that pharmaceutical and health care companies may be among the more strategic givers, but the small sample of such companies in the study makes the drawing of more general conclusions problematic. This would also be a worthwhile research opportunity in this area.

Notes

1. The Percent Club is a part of Business in the Community, and members are required to give 0.5% of pretax profits, in either cash or as in-kind donations, to charity.

2. Excepting the requirement under the U.K. Companies Act since 1967 to disclose the cash amount given away to charitable causes.

3. *The Guardian*'s Giving List for 2002 produced a figure slightly different to this estimate. Differences are probably due in part to measurement differences (the Giving List claims to measure some noncash donations) and a small number of ambiguities as to whether giving is to U.K.-based causes or global causes. Only giving to U.K. causes is reportable under Companies Act provisions.

4. Section 19, Companies Act (1967) and updated Schedule 7, Companies Act (1985), "Political and Charitable Gifts." "If the money given exceeded £200 in amount there shall be

contained in the Directors' Report for the year, the purposes and amount of money given." This requirement does not cover donations made in kind and in noncash terms. If these were also reported at their full value, the overall donations figure would be higher.

5. Rules produced during the course of a content analysis experiment to minimize stability errors, that is, to ensure that coding decisions are consistently applied throughout the course of a content analysis process. A test–retest procedure on a sample of narratives is capable of testing the reliability of disambiguation rules. This was successfully performed at the conclusion of the content analysis procedure described in this article.

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Social disclosure and legitimacy in Premier League football clubs: the first ten years

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Abstract

Purpose – This longitudinal study aims to examine the extent to which football clubs in the Premier League communicate community activities in their annual reports through social disclosure. The research also seeks to examine the relevance and use of the annual report as a disclosure medium by football clubs. The need for social disclosure is examined in conjunction with media coverage of issues affecting Premier League clubs.

Design/methodology/approach – This study is deductive using three main hypotheses to test relevant underpinning theory used within the research. The study uses content analysis of annual report social disclosures of ten Premier League football clubs from 1993 to 2002, covering the first ten years of the Premier League. A questionnaire was used to evaluate the use of annual reports by those clubs. In addition, media reporting data from *The Sunday Times* is examined.

Findings – This study finds that there has been an increase in adverse media reporting concerning football, football clubs and their activities. One way in which clubs have responded to this increased attention and criticism is by expanding their community activities and associated social reporting, although reporting varies between clubs. The study finds that football clubs do value the annual report as an effective means of communication.

Research limitations/implications – The authors acknowledge that some limitations inevitably affect the generalisabilty of this research. The use of content analysis, the precise methods adopted and the reliance on *The Sunday Times* constitute limitations. Nevertheless, the research has shown that clubs do engage with their local communities and have increased their reporting of such activities. The research has implications for those football clubs who fail to report their social activities. Further research could explore, why some clubs disclose more than others.

Originality/value – Football is a visible and important part of the UK economy. The study of social reporting by football clubs is in its infancy and this paper tests and applies relevant accounting theory to that sector. It shows that football clubs have begun to take social disclosure seriously within their annual reports.

Keywords Corporate social responsibility, Football, Annual reports, Communities

Paper type Research paper

Introduction

This paper adds to the literature on voluntary disclosure reporting. Specifically, this paper examines community reporting by English Premier League football clubs between 1992 and 2002. Football clubs community activities represent an important

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part of value added to society through their involvement with football in the community schemes, educational provision and other external roles that they perform such as hospital visits. Conversely, football clubs place their footprint on society in terms of use of resources, stadia development, car parking and match day congestion, football hooliganism, player behaviour and issues relating to players' wages. Football clubs could face adverse publicity arising from these issues, and from their increased public profile, such as television coverage, might be expected to take actions to counter any such criticism. Increased community reporting is a means of emphasising football's positive societal contribution. Historically, football has had an important place in the community and it might be expected that their community role and involvement would be reported to society. These issues are explored in more detail in the section below on theoretical development.

Motivation for football sector study

Research into football clubs is justified for three reasons. First, football is a visible and important part of economy thus it is important to examine this sector. English clubs generated income of almost £1.7bn (of this premier league clubs generated £1.25bn) in 2002/2003 contributing around £550mn taxation revenues. Since, the advent of the Premier League in 1992 clubs have invested in excess of £1bn of capital investment in stadia (Deloitte and Touche, 2000-2005, Annual Reviews of Football Finance).

Second, and of particular relevance to this study, football has its origins in the community. Thus, it makes sense to examine community reporting within the football sector. Football should be accountable to the community which it derived from in the first instance. In general, professional football clubs were formed around the turn of the twentieth century and had a close association with their local communities, either through the church, local schools or local employers. For instance, Arsenal (1886) was formed by workers at The Royal Arsenal, Woolwich, Aston Villa (1874) from members of the Villa Cross Wesleyan Chapel, Everton (1878) from St Domingo Church Sunday School and Southampton (1885) from the young men's association of St Mary's Church. This community history is explicitly recognised by Aston Villa in their 2002 annual report (p. 10). "Aston Villa is a global name deeply rooted in our community, and we continue to nurture relationships with local people that stretch back generations." Such community origins are more generally noted by the Football Task Force (1999. p. 8) report, which stated that "football clubs in England have deep roots in their communities". This view of community relationship is supported by authors such as Morrow (1999, p. 176) who asserted that "it has long been held that football clubs are an important element within local communities", and Morrow (2000, p. 65) "clubs have a deep rooted identification with a particular city or region and hence community".

Finally, in recent years, the legitimacy of football is being increasingly questioned. There have been issues about the business side of football, the payments made to footballers (signing on fees and wages), the behaviour of players and allegations concerning the racism and hooliganism of fans. A number of writers have raised these issues, for instance: "the English game displays all the symptoms of inequality, short-termism and greed" (Lee, 2001, p. 32). Concerns about football spending were also raised in the Deloitte and Touche (2000, p. 4), Annual Review of Football Finance that stated:

> [...] this really is a golden opportunity to put things back on an even keel. We dearly hope to see investment in (among other things) community and fanbase programmes. We worry that

> a lot of it [money] will fairly quickly trickle through the club's fingers to the players and their agents.

If football is to maintain its contract with its communities then it needs to demonstrate an open and accountable relationship.

The rest of this paper proceeds as follows. In the next section, the authors discuss the theoretical perspective adopted. Three hypotheses are then developed in relation to community disclosure which includes discussion of the research design used to test the hypotheses and the methods selected. Results are then discussed followed by conclusions and suggestions for further work.

Theoretical development

There is increased pressure on all businesses to improve their social accountability as evidenced by the establishment of stock market indices such as FTSE4 good in the UK. Companies and organisations are searching out ways by which they can assert their legitimacy as they become faced with an increasingly critical and questioning environment.

Legitimacy theory is typically utilised in the literature, to help, explain social and environmental disclosures (Patten, 1991; Deegan and Gordon, 1996; Deegan, 2002; Milne and Patten, 2002; Campbell *et al.*, 2003) and it is equally suitable to explain social disclosures. It assumes that a social contract exists between society and the organisation and that in some way organisations, which damage that contract, need to repair or reconstruct it in some way so as to obtain societal approval (see in particular Shocker and Sethi, 1974).

The question as to what is meant by legitimacy theory and legitimation is explored in detail by Suchman (1995). Clubs may wish to provide a fuller picture of performance rather than just a financial one. This may be because their performance is poor or because they wish to divert attention away from other financial issues such as players' wages, entrance fees or environmental footprint concerns (such as stadia development), all of which raise questions about legitimacy. Lindblom (1994) asserted that legitimacy concerns provided a motivation for increased social disclosure by organisations that are potentially affected by those concerns.

The paper examines whether the Premier League faces problems of legitimacy. Football clubs have arguably queered their pitch with society because of a number of recent activities associated with the game and the players. These misdemeanours include issues to do with footballers' wages, rising entrance prices, restricted entrance policies (season ticket only), football hooliganism and violence (on and off the pitch), racism and the whole perception of "new commercialism" (Hamil *et al.*, 2000, p. 20ff) taking football away from its societal roots.

Lindblom (1994) described four possible legitimation strategies. These briefly comprise:

(1) an attempt to emphasise future plans of the organisation to rectify past ills;

(2) an effort to change how society perceives past ills;

(3) an emphasis on other good acts which are not necessarily related to past ills; and

(4) to try to change society's expectations about how organisations should behave.

The strategy which is most relevant to this paper is number three. In strategy three, football clubs would disclose community information in order to change society's perceptions about football. The "relevant publics" are informed about whole areas of the club's activities via increased disclosure. This distracts readers away from the negative issues described above (such as hooliganism, racism, footballers' wages and behaviour) and any adverse media reporting by focusing on more positive issues. Thus, constituents are taken away from the bad actions and related publicity to the good (e.g. working with the disadvantaged in the community). Thus, the authors expect, a priori, football clubs to disclose information which informs society about their societal activities and distracts attention from other activities or performance that are less admirable.

The source of these threats to legitimacy are often media related (O'Donovan, 1999; Brown and Deegan, 1998; Deegan *et al.*, 2000) and it is from such an assertion that this paper is developed. "Evidence indicates that management reacts to adverse media coverage and use corporate disclosures as a strategy to alleviate the potential adverse effects caused by negative media coverage" (Deegan *et al.*, 2000, p. 105).

Other studies have examined social disclosure in relation to either individual companies or sectors (see for instance Patten, 1992; Ahmed and Courtis, 1999; Deegan *et al.*, 2000, 2002). Deegan *et al.* (2000, p. 101) found that "organisations utilise their annual report as a means of influencing society's perception of their operations" and further Deegan *et al.* (2002, p. 312) comment "... that management release positive social and environmental information in response to unfavourable media attention". In addition to legitimacy theory, media agenda setting theory is relevant to this paper. This theory suggests an association between media attention to certain issues and how important these issues are perceived to be by the public at large, see Deegan and Unerman (2006) for further discussion, in particular pages 283 and 302, note 11. According to Deegan and Unerman, "increased media attention is believed to lead to increased community concern for a particular issue" (p. 283). In addition, Brown and Deegan (1998) found that higher media coverage was associated with increased disclosure of environmental issues. From this, there is an overlap of media agenda setting and legitimacy theories in that the media may highlight a particular issue which leads to increased public awareness that a company then responds to by increased disclosure so as to maintain its legitimacy. Both Brown and Deegan (1998) and Deegan *et al.* (2000) examined adverse media coverage of issues that affected a sector in general and the individual company responses through increased disclosure that were subsequently made. Brown and Deegan (1998) examined general media coverage of environmental issues and the subsequent environmental disclosures made by companies in those industries most affected. This research was conducted using data from five years over a 13-year time period. Deegan *et al.* (2000) examined specific environmental disasters (such as Exxon Valdez and the Moura mine explosion) and the reactions by companies, through increased social and environmental disclosures, across the relevant whole sector.

This paper adopts a similar approach and examines whether there has been an increase in adverse media attention concerning Premier League football clubs and the associated increase in community disclosure as a response. The media attention to issues such a players wages, fees to agents and merchandising affects the sector as a whole and is not necessarily confined to one or two individual clubs. Through this research, this study extends previous work to a sector which is relatively unresearched in the accounting literature despite its public visibility.

Hypotheses
Based upon the public visibility of football and its high level of press coverage, the first hypothesis tests whether football has a legitimacy problem arising from adverse media coverage:

H1. Levels of adverse coverage of football in newspapers increased over the first ten years of the Premier League.

If this hypothesis is held then according to media agenda setting theory this would indicate increased societal concerns about football. This in turn would imply a greater need for clubs to repair their legitimacy and would suggest that clubs would increase their community disclosures over the period of study.

Many accounting studies, typically, make use of the annual report but there are a number of other reporting vehicles available. These include a separate community report, the match day programme, the club's web site and so on. Web sites are an important communication media, but for football clubs during this period there were issues with full access via subscription and availability over the full period. The annual report is a permanent document which is easily located and referred to (particularly, at some time in the future when other documents are not so easy to trace) and it is "the most widely used and accessible public document issued by companies" (Cross and Djajadikerta, 2004, p. 12). Morrow (2005, p. vi) also claims (writing about the business of football):

> [. . .] the annual report is an important document; a mass communication device capable of providing information to a wide range of groups and of discharging accountability. In particular, narrative reporting in annual reports provides a convenient route for clubs to convey information to interested stakeholders who may not always have the expertise in interpreting financial statements.

In order to further substantiate this claim *H2* was developed as follows:

H2. Football clubs regard the annual report as a key reporting document to stakeholders.

H3 is derived from *H1* and *H2*. If there are increased concerns about clubs' legitimacy (*H1*) and football clubs utilise the annual report (*H2*) to address, these concerns then the authors would expect levels of community disclosure in annual reports to increase over time:

H3. Levels of community disclosure in football clubs' annual reports have increased over the first ten years of the Premier League.

Research design
A ten-year research period was identified between 1993 and 2002. The start year, 1993, marked the formation of the English Premier League (season 1992-1993) and a ten-year period was chosen to provide sufficient longitudinal depth to the research. This also allowed the selection of all contiguous Premier League clubs over that ten-year period. Owing to relegation (and a shifting Premier League composition) the number of clubs would decline, if the period were further extended. For this reason, the time period was as selected.

In relation to both *H1* and *H3*, a content analysis approach was selected. For *H1*, the first issue to be addressed was to determine the appropriate location and measurement of media reporting. A study undertaken by Ivankovic (2004) concluded that, *The Times* was the most suitable paper in the UK for the purpose of content analysis due to its wide distribution and influence. As most football matches occurred on a Saturday afternoon, it was felt most appropriate to use *The Sunday Times*. Although, the authors recognise the limitation of this, *The Sunday Times* is the highest selling broadsheet with a circulation of 1.3mn (July 2005). Owing to the selection of a Sunday newspaper, all weeks across all ten years of the study could be inspected. This was done using library, microfiche and hard copy holdings. Relevant sentences were identified using a content analysis approach (Milne and Adler, 1999). The use of sentences rather than words is appropriate for this study because words have no meaning on their own and by counting sentences the relevance of the search term is easily verified. Appropriate disambiguation and coding rules were developed and an initial three-month pilot study was performed.

In relation to *H3*, the study examined the annual reports of the ten contiguous Premier League clubs from 1993 to 2002. One of the problems inherent with the research in the football sector is the changing composition of leagues because of promotion and relegation. Owing to the financial consequences of this, changes in attendance, playing squads, sponsorship deals, television and media coverage, only those clubs had had been contiguous members from 1993 to 2002 were selected as part of the study. This resulted in ten clubs being used: Arsenal, Aston Villa, Chelsea, Everton, Leeds United, Liverpool, Manchester United, Newcastle United, Southampton and Tottenham Hotspur. The annual reports were obtained directly from all of the clubs to cover the annual reports for every second year, 1994, 1996, 1998, 2000 and 2002. This gave a longitudinal dataset that could be matched against *The Sunday Times* media data.

In order to analyse their community reporting, a content analysis of the financial statements was carried out. Once again, sentences were used as the unit of measure. Where sentences dealt with two issues half sentence per issue was counted.

Discussion of content analysis technique

Content analysis is a way of categorising various items of text for the purpose of analysis. The approach taken should be replicable by other researchers. Milne and Adler (1999) discussed this in relation to social and environmental accounting. For a general discussion on content analysis, see Boyatzis (1998) and Krippendorff (2004). According to Milne and Adler (1999), Krippendorff identified three types of reliability. First, stability refers to a coder being able to code the data consistently over time. This can be a problem where a coder becomes more expert in their coding and thus codes something inconsistently over time. Although, Milne and Adler (1999) report it as being the weakest (of the three measures) it is not unimportant in attaining reliability of coding. Stability can be improved by producing rules (called disambiguation rules) that the coder can refer to throughout the coding process and facilitates consistency.

Consistent with the approach taken with the media reporting, a pilot study of 2002 annual reports was undertaken by the authors. Inter coder reliability was 91 per cent in relation to the annual reports and 95 per cent for *The Sunday Times* study. Initial training of two coders by the authors facilitated the high levels of reliability. Where differences were found further scrutiny of either the annual reports or the newspapers was undertaken.

In order to test *H2*, a questionnaire was designed and sent to all current Premier League clubs as of season 2002-2003. Replies were received from 14 clubs (70 per cent response rate). The clubs were asked what activities they undertook, the reasons for their community involvement, whether or not the community activity should be reported and where it was reported.

Results and discussion

Hypothesis 1

This hypothesis examined the extent to which adverse coverage in *The Sunday Times* of football clubs changed over time. The results are displayed in Table I. Although, some positive sentences were reported, it is clear that the net effect is negative. In particular, the number of negative sentences has increased substantially over time by approximately 100 per cent.

Adverse media coverage addressed players involved in violence on the field and a range of off-field issues such as alcohol- and drug-related incidents, excessive wage demands, sex scandals, overpricing of tickets and merchandising, inappropriate comments made by directors and finally, hooliganism and racism.

Although, football hooliganism has apparently experienced a long-term decline since the late-1980s (Chester, 2001, SNCCFR) evidence suggests that hooliganism associated with football is now organised before and after games (Chester, 2001) and in fact, it appears that hooliganism has increased (Pearson, 1998). The reasoning behind the increased level of media coverage is that paper circulations are boosted as stories have higher impact (O'Higgins and Pearson, 2001). The situation is perhaps exacerbated by the media as they have been accused of inciting hooliganism through the use of inflammatory headlines (O'Higgins and Pearson, 2001). All this suggests that clubs and players face increased demands to legitimise their activities and report more positive engagement with community activities.

Hypothesis 2

The validity of the annual report as a reporting mechanism by football clubs in relation to voluntary community disclosure was tested as part of the survey questionnaire. Clubs were asked whether and where they reported their community activities. All clubs agreed that such activities should be reported. The most frequently used reporting media were the match day programme and the annual report followed by the club's web site, local press and finally, local radio and television. The authors found that clubs demonstrated their engagement with the community. For example, all clubs participated in school visits, worked with disabled people and were involved with anti-racism activities. About 93 per cent of respondents engaged in working with disadvantaged people, ethnic integration, helping young offenders and supporting charity events and offering IT facilities. All clubs agreed that their community activities need to be reported and the two most appropriate disclosure vehicles were the match day programme and the annual report. These were ranked ahead of the club web site, local newspapers and radio/TV.

Year	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Adverse comment	396	456	583	985	577	741	760	778	767	784
Positive comment	11	18	30	25	37	22	29	15	25	34

Table I. Football: adverse and positive sentences in *The Sunday Times* 1992-2001

This affirms this study's decision to use the annual report and confirms *H2* that the annual report is used by clubs to inform stakeholders about club community activities.

Hypothesis 3

Regarding the final hypothesis (*H3*), the authors found that over the ten clubs community disclosure ranged from 11 sentences in 1994 to 153.5 sentences in 2002. This is shown in Table II.

The increased disclosure is consistent with clubs becoming more involved with their communities as a response to adverse media publicity elsewhere. To test this, a correlation with a one year time lag between media reporting and community disclosure was performed. This resulted in 87.4 per cent correlation. The general increase by clubs in their community efforts is evidenced by a report by the football in the community scheme (McGuire and Fenoglio, 2004, p. 2) which stated that:

> [. . .] the general trend (1994 to 2004) seemed to be one of improved relationships between the clubs and the schemes. Many senior officers felt that club officials were now more aware of community relations generally and knew the positive effects that a good, vibrant scheme can have on a club's image.

Image management via community activities can thus be utilised by clubs as a response to, or distraction from, adverse publicity that would otherwise be harmful to the clubs reputations. Recognition of the increase in community activities and the increased level of reporting is also clearly shown at an individual club level exemplified by Chelsea (2000, p. 4):

> [. . .] the Chelsea Football in the Community Scheme was formed as a one man operation in October 1992. Today it has 6 full time officers [. . .] and in the year 2000 over 13,000 children will have benefited from this Chelsea Community Initiative.

There had been no earlier reporting of this by Chelsea prior to 2000. Some clubs were more explicit in their reporting by recognising the impact and benefits of their community involvement, partly to further their own commercial interests. For instance, Tottenham Hotspur (2002, p. 11):

> If we are successful in our planning application, once the new facility at Abridge is in use, the current Spurs Lodge training ground will become the home for our successful Football in the Community scheme.

Further to this:

> [. . .] when Liverpool FC recently announced their new stadium plans, they took the opportunity to re-assess many aspects of the club and are delighted at how they have forged stronger links with the local community as a result (*Football in the Community* magazine, Summer 2003, p. 8).

Such examples show the use of community involvement as a means of partly justifying, and diverting attention away from, continued facility expansion.

Table II.
Community disclosure by Premier League football clubs (sample)

Year	1994	1996	1998	2000	2002
Sentences	11	14.5	25.5	76	153.5
Percentage increase	N/A	31.8	75.9	198.0	102.0

Other clubs were concerned with demonstrating their involvement within society and by doing so paying society back. This raises the question as to what they need to pay back, if there were no legitimacy concerns, and hence their desire to re-emphasise their community links. At a club level this is shown by extracts from Liverpool (2000, p. 13) "partnership initiatives (such as Reduc@te) aim to give something back to our local communities" and Manchester United (2000, p. 6):

> Manchester United is committed to working on programmes which are able to make a real impact on the community. We also recognise that we have an obligation to play a positive role in our local community.

Across the sample of Premier League clubs, the greatest increases were from 25.5 sentences in 1998 to 76 sentences in 2000 and from that figure to 153.5 in 2002. A total of 55 per cent of all disclosures were made in the last year (2002). Disclosure did not really become significant until 1998. Typically, clubs showed fairly dramatic increases in disclosure in 2000 or 2002 from a low base. For instance, Arsenal and Aston Villa, 28 and 18.5 sentences, respectively, in 2002 (both very little in preceding years). This is borne out by the level of new schemes entered into by Arsenal and its 2002 reporting (p. 12). Firstly, "Arsenal Double Club: Established in 1998 the Arsenal Double Club is an education and football programme which offers literacy, numeracy, IT and football coaching." Secondly, "Arsenal Sport and Learning Project: In September 2001, Arsenal together with Islington Council, launched an exciting and innovative project for year 10 students from Islington schools." Finally, "Gunners in Islington: In April 2000 Arsenal in the Community joined up with local residents, the Metropolitan police and other community organisations to establish the 'Gunners in Canonbury' scheme."

This paper has established that clubs engage in community activities and that they have a need to report those activities. The authors' survey of the clubs found that the most prominent reason stated for community involvement was to "pay back the community" thus explicitly acknowledging their relationship with the community and the need to demonstrate accountability. The reporting of these activities has been utilised to deflect media attention which is consistent with Lindblom's third strategy.

Conclusion, limitations and further work

Football clubs have begun to face questions about their legitimacy. Concerns about the recent commercialisation of the game, player wages and player behaviour, questions about the environmental impact of stadia, academy and associated developments, hooliganism and racial abuse at grounds and their environs, have meant that there are significant questions about the legitimacy of football clubs and their position in society. Using a theoretical framework constructed on media agenda, setting and legitimacy theory. this paper has shown a matched increase in social disclosure by football clubs following an increase in adverse media coverage concerning the football sector, and the Premier League in particular. The threat to legitimacy is sector wide and relates to issues such as excessive player wages, payments to agents, fan behaviour and merchandising. This sector wide response to a potential legitimacy threat is consistent with earlier disclosure studies in other industries, for instance Brown and Deegan (1998) and Deegan *et al.* (2000).

The study of social reporting by football clubs is in its infancy but this study has shown that football clubs have begun to take disclosure seriously and that some of the larger clubs make significant amounts of social disclosure. Whilst, the study has shown that all clubs have increased community disclosure, there is still a disparity over the individual level of such disclosure. Further research should investigate why some clubs disclose more than others. It remains to be seen whether in time all clubs will follow the lead made by some of the clubs referred to in this study.

The authors acknowledge that there are some limitations in a study which utilises annual reports and counts sentences. Unerman (2000) concluded his methodological study into content analysis by explaining that annual reports do not provide a complete picture of social disclosure. The authors feel that the permanent record of annual reports justifies their use particularly as web sites are often overwritten. He further articulated that sentence counting which ignores "pictures, graphics and different typeface sizes" (p. 678) is likely to result in an incomplete picture of social reporting. However, the authors believe that the increased reliability which sentence counting offers avoids the subjectivity which including these other features would invariably involve. The authors accept that sentences can comprise a number of parts and some details are inevitably lost by ignoring statements that were smaller than a half of a sentence, on balance the authors feel that to include them would be over-resolving the data set.

The authors acknowledge that this is an initial study into social reporting in a particular sector. It has provided valuable insights into social disclosure by Premier League football clubs and provides a useful platform for further work that could involve looking at such disclosures made by all professional football clubs in the English leagues, as well as a cross country comparison.

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Criteria for Responsible Business Practice in SMEs: An Exploratory Case of U.K. Fair Trade Organisations

Geoff Moore
Richard Slack
Jane Gibbon

ABSTRACT. This paper develops a set of 16 criteria, divided into four groupings, for responsible business practice (RBP) in Small and Medium-Sized Enterprises (SMEs) drawn from the existing SME/RBP literature. The current lack of a general set of criteria against which such activity can be judged is noted and this deficit is redressed. In order to make an initial assessment in support of the criteria so derived, an exploratory feasibility study of RBP in U.K. Fair Trade organisations was conducted. The findings from this study show that most but not all of the RBP criteria seem to be applicable to U.K. Fair Trade organisations but it is recommended that the complete set of criteria continues to be used in further research until such time as there is a general consensus as to which criteria are appropriate. Implications for RBP in small businesses in general, and for Fair Trade organisations in particular, are drawn out and suggestions for further research are identified.

KEY WORDS: corporate social responsibility, Fair-trade, Fair Trade, responsible business practice, Small and Medium-Sized Enterprises

Introduction

This paper focuses on developing a set of criteria for responsible business practice (RBP) amongst Small and Medium-Sized Enterprises (SMEs). While there is a developing literature in this area, there is currently no agreed set of criteria against which such activity can be measured. Without such criteria research in this area could be conducted on a basis which makes comparison difficult. Hence, the initial contribution of this paper is to construct such a set of criteria from the small business ethics literature.

In order to make an initial assessment of the criteria so derived, they were applied to U.K. Fair Trade organisations. Given that Fair Trade organisations have a requirement to abide by RBP criteria such as those set by the International Fair Trade Association (IFAT), such organisations provide a suitable purposive sample against which to initially

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test the criteria. Equally, no such study has yet been undertaken on Fair Trade organisations and so the paper also makes a contribution to the developing literature on Fair Trade.

The paper, then, proceeds as follows. First, the literature related to RBP in SMEs is reviewed and from this a set of criteria is derived, together with a number of other variables to be measured in such research. As the sample group is composed of Fair Trade organisations there is a brief review of the Fair Trade literature before the method for the exploratory study is described and the results reported. A discussion follows and implications both for RBP in small businesses and for Fair Trade organisations are drawn out. Suggestions for further research are identified.

Responsible business practice in SMEs

Although we have used the term RBP, and defend its use below, the literature on RBP in SMEs is, of course, set within the broader literature on corporate social responsibility (CSR). The literature on CSR and SMEs is limited when compared with the equivalent literature related to large business, but it is now burgeoning – see Moore and Spence (2006) for a summary. There is a general consensus, however, concerning the danger of simply taking CSR as related to large companies and applying it to SMEs (CSR Magazine, 2002; Fassin, 2008; Graafland et al., 2003; Jenkins, 2004; Southwell, 2004; Spence and Rutherfoord, 2003). While SMEs are, themselves, not a homogenous group, it is clear that small is different and, generally, informal (Fassin, 2008; Graafland et al., 2003, p. 57). In some cases there is a link between the owner–manager and the firm and, hence, personal choices can affect activities at the firm level (Spence and Rutherfoord, 2001, p. 127). There is, therefore, at least an implied link to entrepreneurship and entrepreneurial activity (Fassin, 2008; Fisscher et al., 2005; Hannafey, 2003; Lahdesmaki, 2005; Wempe, 2005 and see also Lepoutre and Heene, 2006, pp. 261–262), although this is not explored here directly since it relates more to a particular type of business person, (who generally pursues a growth and profit-maximising strategy), than to SMEs' attempts at integrating CSR within their activities.

SMEs are not only informal and in some cases owner–manager driven, but another factor emerging from the literature is that social relationships and networks can be an integral part of the business (Spence and Rutherfoord, 2003, p. 2). Indeed, Lawrence et al. (2006) refer to the use of networks as a method of encouraging SMEs to develop sustainable practices. Links to the community may well therefore be both an intrinsic part of how SMEs behave, and something to be encouraged, rather than something to be regarded as a 'bolt-on' activity. However, Curran et al. (2000) and Besser and Miller (2001) both found that community links are not necessarily such an intrinsic part of SME activity, so that such links, while desirable from a CSR viewpoint, cannot be assumed. The main point to emerge here, however, is that SMEs may well engage in socially responsible practices without necessarily viewing such activity in this way. Indeed, while an early study showed that half of the European SMEs were involved, to different degrees, in external socially responsible causes (European Commission, 2002), the extent to which these businesses would explicitly articulate that they were involved in such activity was less clear.

Terminology

That SMEs may well be doing CSR without knowing it or calling it CSR is linked to the issue of terminology. Southwell (2004, pp. 100–101) discusses this and the problem of applying CSR directly to SMEs. While within the study she reports ''corporate social responsibility'' was the most common phrase, it was not seen as the most appropriate. Jenkins (2004, p. 52) suggests ''business community interaction'' but this seems unduly restrictive to one particular dimension. Murillo and Lozano (2006, p. 237) argue for ''responsible competitiveness'', a term which is recognised in a recent European Parliament resolution on CSR (though not specific to SMEs) (European Parliament, 2007, p. 4), while Lepoutre and Heene (2006) use ''small business social responsibility''. However, ''responsible business practice'' was a reasonably popular alternative term in the study on which Southwell reports and, when combined with her suggestions of emphasising the totality of this activity and similarly emphasising the pragmatic value to the business of such engagement, it seems to be appropriate. The same term also finds recognition in the European Parliament resolution referred to above (European Parliament, 2007, p. 5). This is therefore used henceforth and abbreviated to RBP.

Classifications

A further issue in the literature is that various attempts have been made to classify SMEs in relation to RBP. Southwell (2004, pp. 99–101) classifies SMEs into six different types: Ben and Anitas (social enterprises); Arthur Daleys (financially oriented); One-offs (relatively minimal experience of engagement with RBP); DIYers (fiercely independent); smart pragmatists (recognise the business benefits of RBP) and enlightened pragmatists (similar to smart pragmatists but "motivated by broader, long-term, societal goals" (*ibid.*, p. 99)). Spence and Rutherfoord (2001) provide a different classification based on profit-maximising versus profit-satisficing *perspectives* on one dimension and socially active versus socially inactive *practices* on the other. Their resultant 2×2 matrix identifies profit maximisation; subsistence; enlightened self-interest and social priority as four different types. A further classification is based on a simple dichotomous division between "champions" for RBP (Jenkins, 2006) or, alternatively, SMEs that are "active" in social and environmental actions (Murillo and Lozano, 2006) compared with those that are neither champions nor active.

Strategies for organising RBP

Graafland et al. (2003) draw on the work of others and identify three different strategies for organising ethics (whether in SMEs or otherwise). First is the compliance strategy where the focus is on required behaviour. Second is the integrity strategy that relies on the responsibility and integrity of individual employees but based on clearly defined core values and training to enable employees to apply these values. Third is the dialogue strategy which pays attention to the expectations of the stakeholders of the firm and "focuses on responsiveness to the ideas, interests and values of others" (Graafland et al., 2003, p. 47). Although these strategies are complementary, their research findings suggest that, where any kind of strategy is used by SMEs, the dialogue strategy predominates (37%) over the integrity strategy (19%) and the compliance strategy (7%).

This suggests that SMEs may be more "socializing" in their approach to RBP, incorporating "a dialogic approach to accountability based on reciprocal relationships of mutual dependency" (Spence, 2004, p. 120). The alternative "individualizing" approach would rely on more formal accountability mechanisms such as "social and environmental accounts and audits and corporate governance and various legal frameworks to protect processes of disclosure of unethical practices" (*ibid.*, pp. 119–120). Spence (*ibid.*, p. 125) confirms the socialising nature of accountability to employees through dialogue and continuity of employment and also integrity towards clients and competitors where, particularly in relation to clients, relationships with the owner–manager may well be on first name terms. Both Graafland et al. (2003) and Spence (2004) therefore indicate the predominance of dialogic relationships in SMEs with informality rather than formality (Gray et al., 2006) likely to be evident in relation to RBP in SMEs. Fassin (2008), arguing from a practitioner perspective, is vehement in his defence of retaining the informality of RBP in SMEs.

Criteria for RBP in SMEs

With this as background we turn to identifying a set of criteria against which to judge RBP in SMEs. While the informal, dialogic approach to RBP in SMEs might seem to suggest that establishing criteria runs counter to this by apparently formalising RBP, it is clear both from the literature and from practice that some criteria can be established, and certainly for research purposes such criteria are clearly necessary. The establishment of such criteria does not, of course, determine the research method that might be used to identify whether the criteria are being satisfied in any particular SME (see Moore and Spence (2006) and Spence and Rutherfoord (2003) for discussions of appropriate research methods). Although in the exploratory study reported below the use of website disclosure and self-reports are used to determine whether the criteria are being met, ethnographic methods may well be suited to exploring the way in which some of the criteria are actually met. Equally, surveys might be an appropriate method.

In determining a set of criteria, then, in addition to items to be included from the preceding discussion, the most helpful criteria are found within European Commission (2002), Graafland et al. (2003), Jenkins (2004), Lahdesmaki (2005), Southwell (2004), Small Business Service (2002) and Spence (2004). Tencati et al. (2004) also provide a comprehensive list of criteria, although these are not specific to SMEs. Jenkins (2006, p. 248) and Perrini et al. (2007, pp. 297–298) also provide lists of criteria. Neither of these papers was available at the outset of this research, though in both cases the broad categories (mainly stakeholder groupings) are consistent with those used here. Drawing from the available sources, a comprehensive set of criteria containing 16 variables was derived,[1] and is shown in Table I. In drawing together the RBP criteria it was immediately noted that several of these may have little relevance to the U.K. as opposed to the European context from which they were drawn. However, it was decided to include all the criteria in the exploratory study and to comment further once the empirical data from the study was available.

Four key groupings emerged from the criteria as follows:

- Governance of RBP
- Employees in the organisation
- Stakeholder relationships
- External reporting and monitoring

The 16 criteria are not split equally between the four identified groupings, but rather each grouping reflects the common element arising from a collection of discrete variables. The groupings demonstrate the holistic approach to RBP from an internal organisation perspective (governance and employees) and to the external environment (stakeholder relationships and reporting and monitoring). Within the current SME literature itself the groupings identified are recognised but as separate areas. For instance, concerning governance and SMEs, see Abor and Biekpe (2007) and Gray (2006); for employees, see Devins et al. (2004) and Bacon and Hoque (2005); for stakeholder relationships, see Kusyk and Lozano (2007) and for reporting, see Fassin (2008). Drawing these previously discrete groupings together provides a suggested framework with a holistic view of RBP in SMEs.

Other variables

In addition to these criteria other variables need to be considered. Graafland et al. (2003, p. 52), in their survey of large and small firms in The Netherlands, found that in all the instruments they identified for organising RBP (code of conduct; ISO 9001/14001 certification; NEVI code (a code of conduct for suppliers); social report; staff handbook; confidential person; ethics committee; member of the board responsible for ethical issues and ethical training) small firms typically used these far less than large firms. When correlated against size (number of employees) there was a statistically significant difference ($p < 0.05$) in relation to ISO certification, social reports, staff handbook and confidential person. Thus, while these criteria are potentially appropriate for SMEs in general it would not be surprising if there were to be a correlation with size, with differences in RBP between micro, small and medium-sized enterprises. Independence is clearly also an issue with Graafland et al. (2003) finding that subsidiaries generally performed better on most of the instruments, indicating that a form of direct 'ethics supply chain' has an effect on RBP. Other studies in the area of corporate versus social performance (see Moore (2001), Moore and Robson (2002) for a summary) have confirmed the size relation but also found age to be a factor in social performance among large firms, and this might similarly be expected to be a factor for SMEs; the older an SME the more likely that RBP might have become embedded within the firm. Thus, size, independence and age are also variables to be included in any empirical study.

Fair Trade organisations

In order to make an initial empirical assessment of the criteria for RBP in SMEs that had been derived it was decided to focus on U.K. Fair Trade organisations. To contextualise Fair Trade, the

TABLE I

Criteria for RBP by grouping

Criterion		Description	Search terms
Governance of RBP			
1	Profit motive	Degree to which the maximisation of profit is not a clear priority or is regarded as a constraint rather than a priority	Profit(s)
2	Code of conduct	Code of ethics, values statement/rules of conduct	Code of conduct
3	Ethics committee	A committee with responsibility for implementation and monitoring of a code of conduct or ethical matters in general	Ethics committee
4	Board member	Member of the Board with specific responsibility for ethics issues	Ethics director
Employees in the organisation			
5	Staff handbook	Internal document clarifying the position of employees on labour conditions, rules, etc.	Staff handbook
6	Training for employees	Training in relation to codes of ethics and their application	Ethics training
7	Responsibility towards employees	Skill development Work-life balance Health and well-being	Employee Employee welfare Employee skills Employee health Employee well-being Staff Staff welfare Staff skills Staff health Staff well-being
8	Confidential person	Someone independent to whom employees can turn	Mentor Confidential person
Stakeholder relationships			
9	Responsibility towards the environment	Environmental policy Recycling Reducing waste	Environment(al) Sustainable(ility)
10	Responsibility towards the community	Support sporting activities Support cultural activities Support health and welfare activities Support educational and training activities Give preference to personnel from socially deprived groups when recruiting Participate in public affairs or political process on behalf of the enterprise	Community(ies)
11	Responsibility towards suppliers	Ethical sourcing policy and practices	Supplier(s) Producer(s)
12	Responsibility towards customers/clients	Product/service safety Product/service quality Pricing/value for money Customer satisfaction Marketing information	Customer(s) Client(s)

TABLE I

continued

	Criterion	Description	Search terms
13	Responsibility towards competitors	Behave responsibly in relation to competitors Collaborate appropriately	Competitor(s)
External reporting and monitoring			
14	Certification	ISO 9001 (quality) ISO 14001 (environmental) Investors in people	ISO9001 ISO14001 Investor(s) in people
15	Communication with stakeholders	Communication with: Employees External shareholders Customers Suppliers Government (local or national) Media	Stakeholder(s)
16	Social report	Publication of an (annual) audit of social and environmental impacts	Social report Social account(s) Environmental report

U.K., which has the largest retail value of Fair Trade goods carrying the Fairtrade Mark in Europe (Krier, 2006, p. 15), had an annual turnover of such goods of £493 m (circa €600 m) in 2007 with more than 3000 products available. All major supermarket chains in the U.K. sell Fair Trade products together with many smaller stores and catering operations (www.fairtrade.org.uk, accessed 26 September 2008). A summary of the development, parameters and issues facing Fair Trade from an academic perspective is contained in Moore (2004) and similarly from a practitioner perspective in Wills (2006) (and see also IDC (2007), Moore et al. (2006), Nicholls and Opal (2005) and Raynolds et al. (2007)). In practice, all Fair Trade organisations are small or medium-sized businesses (SMEs) within the generally accepted definition of up to 250 employees (European Commission, 2003)[2] and so provide a relevant population.

The accepted definition of Fair Trade is as follows:

> Fair Trade is a trading partnership, based on dialogue, transparency and respect, that seeks greater equity in international trade. It contributes to sustainable development by offering better trading conditions to, and securing the rights of, marginalized producers and workers – especially in the South. Fair trade organisations (backed by consumers) are engaged actively in supporting producers, awareness raising and in campaigning for changes in the rules and practice of conventional international trade. (FINE, 2001)[3]

This definition has, in essence, two basic components. The first is to provide a working model of international trade that makes a difference to the producers and consumers that engage in it and to do so in such a way that social objectives – better trading conditions, the securing of rights and the development of consumer consciousness in the North – are met (see Hayes (2006) and Hayes and Moore (2005) for an understanding of how the economics of Fair Trade works in practice). The second and more radical component of Fair Trade is to challenge orthodoxy in business practice: to be a "tool for modifying the dominant economic model" (Renard, 2003, p. 91) and encourage it towards more social ends. It is, of course, this second component that links with RBP and suggests that Fair Trade organisations might be expected to fall into the social enterprise, social priority and champion/active categories identified above. Thus, as a homogenous group with an explicitly ethical approach to business, they form a suitable purposive population in which to find evidence of the applicability and use of the RBP criteria.

However, whether Fair Trade as it has emerged into the mainstream is better able to influence conventional business practice remains open to debate. Low and Davenport (2006) argue that rather than the mainstream adopting Fair Trade practices, Fair Trade has simply been assimilated into mainstream commercial trade where it ''will remain a small, lucrative niche'' (p. 322). But with Traidcraft and Cafédirect (two of the case study organisations in this exploratory study) occupying sixth and seventh position among the most ethically perceived brands in the U.K. in a GfK NOP consumer survey,[4] it seems that consumers identify Fair Trade organisations as ethical businesses. The challenge, however, may be to maintain that position against critics who would wish to see them fall from that high pedestal. Hence again the importance of RBP practices within U.K. Fair Trade organisation would seem to be self-evident. We will return to this issue in the discussion.

Exploratory study

For the purposes of this study the Fair Trade umbrella organisation of interest was IFAT since this focuses on organisations and sets standards for membership that have some parallels with more general RBP criteria. (The alternative umbrella organisation, FLO, also provides certification standards but these are focused on products rather than organisations – see Moore (2004).)[5] The nine IFAT standards (IFAT, 2005) that were in place at the commencement of the empirical work involved in this study are shown in Appendix 1.[6] The standards cover: creating opportunities for economically disadvantaged producers; transparency and accountability; capacity building; promoting Fair Trade; payment of a fair price; gender equity; working conditions; child labour and environment. It can be seen from this that these standards follow in some respects conventional RBP criteria, but unsurprisingly have a focus on particular aspects of Fair Trade and its concern with marginalised producers and workers in the South. Within the Fair Trade movement there is a belief that these Fair Trade standards are superior to conventional RBP criteria.[7] However, it is also clear that in some respects the Fair Trade standards differ from such RBP criteria.

The primary data collection for the exploratory study comprised two stages. Stage one was based on website disclosures against the RBP criteria. This was followed up in stage two by direct requests for further information about compliance with these criteria. At the start of the collection period an initial listing of all the U.K. listed IFAT members was extracted from the IFAT membership list (www.ifat.org). For the U.K. there were 16 organisations listed and from this the 11 trading organisations were selected for this study as shown in Table II below.[8]

Given the small number of organisations in the sample, this serves as an exploratory study only to assess the RBP criteria developed above, to provide observations on their applicability to U.K. Fair Trade organisations and more widely to serve as an initial observation on their applicability to SMEs as a whole.

The websites of all the organisations included in the study were reviewed to identify RBP criteria disclosure based on key words. The key words themselves were selected from a prior study of Traidcraft's website and are shown in Table I. Two coding decisions were made against the criteria, firstly a binary present/not present and secondly, where the criterion was present, the number of associated ''hits'' so providing volumetric data. As well as providing some direct outputs, this preliminary disclosure analysis also performed another function in providing an entrée to the organisations themselves.

The second stage of data collection took place after the website coding had been performed and the data analysed. The request to each organisation was partly to comment on the website analysis (which was tailored to each organisation), but mainly to supply existing documents such as annual reports, social reports, or to provide files or other materials. There was no limit placed on which documents or evidence could be supplied, only a request that they should not be written specifically for the purpose of this survey. The responses complied with this request and were consequently a mixture of hard copy documents, comments by e-mail and electronic file attachments.

Non-response bias

Organisations that did not respond to the original request to provide further data were contacted by e-mail a second time and in all five organisations responded. Although the response rate was somewhat disappointing given the personal nature of the approach used, there was no evidence of response bias.

Results

Website analysis

The results of the website analysis against the RBP criteria are shown in Figure 1. The graph shows "Present" referring to whether a website provided disclosure against that criterion. The results are expressed as a percentage of all organisations. Numbers of "hits" (i.e. the number of times a particular criterion was disclosed) are also shown and are reported as a percentage of the total number of hits and thus sum to 100%. Two of the websites were "retail only", i.e. they were directed entirely at selling products rather than giving organisational information. Nonetheless, there was some incidental disclosure even on these sites and, as the public face of these organisations, their results were included in the analysis.

Some criteria, as anticipated, have no disclosure against them which may suggest that these are not culturally appropriate in the U.K. (e.g. having a Board member responsible for ethics). On the other hand, one might expect Fair Trade organisations to have an ethics committee, but this is not the case according to the websites. Environment, community and suppliers dominate the "hits" with employees and customers following. In total, against all criteria for all organisations (i.e. 16 × 11), the disclosure rate was 49.6%.

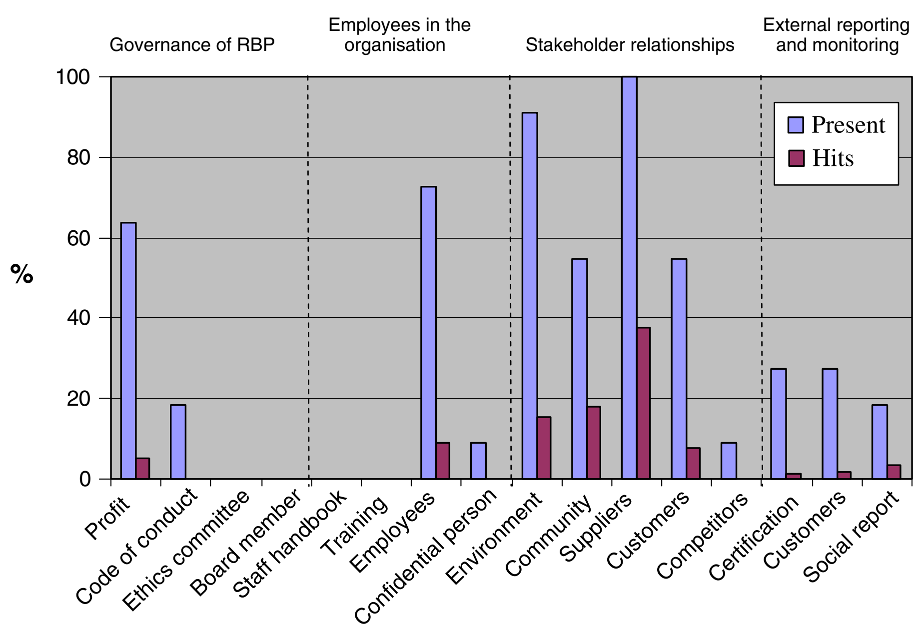

Figure 1. RBP criteria by importance.

TABLE II

IFAT U.K. Fair Trade organisations included in the study

Bishopston trading company	Bookchair company	Cafédirect
Divine Chocolate Ltd	Equal exchange trading	One world shop
Shared earth	Shared interest	Traidcraft
Tropical forest products	Tropical Wholefoods	

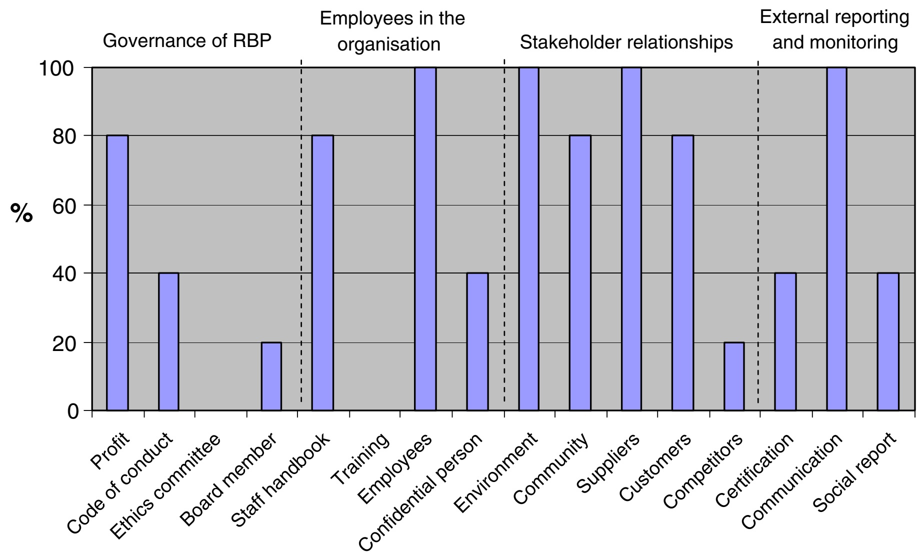

Figure 2. RBP criteria – follow-up respondents only.

Follow-up request for further data

The responses to the request for further data were analysed by considering each comment, document or file in turn and recording evidence concerning compliance against the RBP criteria. While this could be considered as a self-reporting disclosure study, the compliance with the request to provide existing documents and not to answer a survey provides some reassurance that what is being measured is genuinely performance rather than merely disclosure. In this case no volumetric analysis was conducted, the point being to assess whether there was sufficient evidence to show that criteria that had previously been recorded as not met according to the website analysis were, in fact, being met.

The findings were in line with what had been expected. On RBP criteria the compliance rate increased from 32.5% (well below the average for all organisations' websites of 49.6% noted above) to 57.5% following full disclosure. This is a significant rise in itself and to well above the average for all organisations based only on their website disclosure. In particular, criteria related to profit levels, codes of conduct (which could include a values statement), the presence of staff handbooks, responsibility to employees, responsibility to the community (interpreted as local to the organisation in the U.K. rather than communities in developing countries), responsibility to customers and communication with stakeholders all became much more evident where previously the websites had not disclosed very much against these criteria. The results are shown in Figure 2.

In relation to the groupings identified above, the picture is mixed. The governance of RBP is evident to some extent but with no ethics committees. Employees in the organisation is also evident but with no training for employees. Stakeholder relationships was the strongest grouping with only competitors having a limited response. External reporting and monitoring is also evident but, not surprisingly, communication with stakeholders dominates this grouping.

There could be some confusion or reluctance to identify other Fair Trade organisations as competitors rather than collaborators in a movement given the network they form, so it is possible that the low response rate here is explicable. In relation to the two criteria against which there was no evidence, it is entirely reasonable to suppose that for these particular organisations, with their strong ethical basis in being part of the Fair Trade movement, the requirement to formalise ethics issues by an ethics committee, for example, or by providing specific ethics training to employees, is considered irrelevant. That only two organisations had a code of conduct – and in both cases this was a values statement rather than a full code that might be found in larger firms – seems to confirm this. Only two organisations, however, had a confidential person in place to whom employees could turn. In line with good whistle-blowing practice this might be an area for further consideration. That two organisations were engaged in social reporting (and, indeed, one of these – Traidcraft – has won awards for its social reports), suggests that social reporting is not necessarily beyond SMEs, in contrast with Fassin's (2008) claims that social reporting is inappropriate for SMEs.

As noted above, then, these findings confirm what had been expected – that these organisations were, in practice, more fully engaged in RBP activities than their websites had indicated.

Age, size and independence

The organisations are all independent of parent companies, the one exception being Divine Chocolate Ltd. (http://www.divinechocolate.com, accessed 25 September 2008) which is owned by a combination of Kuapa Kokoo (the cocoa farmers which supply it), Twin Trading and Oikocredit (an international development finance institution). In addition, Christian Aid owns preference shares. This interesting structure is unique amongst the organisations surveyed but it does not match with conventional ownership which is the usual criterion against which independence is judged. Hence, no analysis of the results against independence was possible. Analyses against size (turnover) and age (years since foundation) showed no statistically significant correlation for either the website disclosure or the full responses from the five organisations. A larger and more diverse population would, therefore, be needed to enable analysis of these variables.

Discussion

The sample

SMEs can be viewed as a disparate mix of businesses being far more informal in organisational structure, internal reporting and lines of communication when compared to large businesses. Emerging from such characteristics it is fair to say that SMEs are not homogenous, are sometimes driven by owner-manager values, and so can be difficult to compare directly both to each other and certainly against larger businesses. Jenkins (2004, p. 40) has already highlighted this problem with SME research in that "usually underlying these discussions are certain suppositions that may not apply to the average SME".

One aspect of this exploratory study is that the fundamental values of the businesses examined are shared, with Fair Trade values underpinning all the organisations in this study. Within this study, then, there was no need to overlay or identify a values matrix approach around differentiating characteristics as suggested in Southwell's (2004) typology or Spence and Rutherfoord's (2001) classification, referred to above. Thus, as noted above, this sample falls entirely within the "Ben and Anitas" type or the "social priority" class, and could similarly be characterised amongst the "champions for CSR" (Jenkins, 2006). However, this means that the results from this study are not necessarily transferable to other types of SMEs, though they should be directly comparable with other SMEs of their type. However, as a means of exploring RBP criteria the sample was appropriate.

RBP criteria and groupings

That 14 of the 16 criteria derived from the literature were found to be present in at least one or more of the Fair Trade organisations when the detailed follow-up responses were analysed, and that there may be reasonable explanations for the absence of the other two criteria, suggests that these 16 criteria do form a sound basis on which future research in this area might be conducted. While the concern about the formalisation of RBP in SMEs was noted above, it seems that such criteria are appropriate to and observable within SMEs.

However, the fact that the response rate was only 49.6% for the website disclosure rising to 57.5% for the full responses, indicates that only about half of these criteria are satisfied in the organisations studied. However, within the four groupings of criteria that were identified, each has a majority of criteria present. Further studies should both confirm the criteria themselves and give further data on the extent to which SMEs do comply with these criteria.

Particular attention might be paid to those criteria where no or limited evidence was provided of compliance and to other classifications of SME to see whether they satisfy more or fewer criteria. Overall, however, the main contribution of the paper has been met – to derive a set of criteria for RBP in SMEs and to conduct an initial empirical test to confirm their applicability. The grouping of the criteria into internal (governance of RBP and employees) and external (stakeholder relationships and reporting and monitoring) areas may also be useful in emphasising these groupings over individual criteria within them.

Under-reporting of RBP activity

SMEs on their own have been viewed as insignificant in relation to influencing other businesses or stakeholders around them or through the supply chain. Jenkins (2006, p. 243) asserted that ''SMEs remain largely invisible'' in relation to RBP and, if this is the case, then the broadening and adoption of RBP by others is made more difficult as even the champions of RBP remain largely hidden from view. This was borne out by Jenkins' (2006) study which specifically examined SME CSR champions and still concluded that, ''many companies were uncomfortable with the idea of promoting their CSR activities [which was] seen as a ''big business'' thing to do'' (p. 250).

However, as one of the fundamental aims for Fair Trade is to raise social awareness and to challenge the orthodoxy in business practice, the level of reporting and disclosure to help achieve these aims might be expected to be high in these organisations. Moreover, as all organisations in this study have a shared Fair Trade identity from their IFAT membership, the problematic issue of their collective visibility could be reduced due to the public recognition of Fair Trade goods and the Fair Trade brand. Thus, such a collective SME group (a network) could galvanise RBP via a holistic approach rather than through the efforts of single entities. This could lead to a common RBP message, but in order for this message and practice to be seen and adopted by others it would need communication and wide disclosure. A similar approach could be advanced for industry specific or local groupings of SME to promote RBP as a group rather than it reside solely within individual entities.

However, allowing for the tentative nature of the website disclosure results, this study suggests that such dissemination of good practice is not, in general, taking place to the extent that might be expected. That performance for the five respondents in general nearly doubled over their disclosure is evidence of this. This, however, confirms results commonly found in other studies. Jenkins (2006) reported that, ''only three companies [out of 24 in the study] reported on any aspect of their CSR and none reported annually'' (p. 249), and Murillo and Lozano (2006) found ''the companies [all SMEs] … do not appear to communicate their social practices to any great extent'' (p. 236). However, of interest is that one of the companies, Shared Interest, now has a specific reference to CSR on its home page (www.shared-interest.com, accessed 25 September 2008).

Level of RBP activity

The apparent under-disclosure of RBP activity, discussed above, needs to be contrasted with the actual level of RBP performance. Whilst, as noted, some of the criteria – such as having an ethics committee or providing ethics training – may not be appropriate either for these organisations in particular or in a U.K. context, there are a number of possible areas for consideration, based on the responses from the five respondent organisations, in relation to developing RBP activities. These would seem to be important areas for Fair Trade organisations to attend to if their ability to challenge mainstream organisations is not eventually to be undermined.

However, even allowing for these weaknesses, it is not clear from this analysis that Low and Davenport's (2006) argument that Fair Trade has simply been assimilated into mainstream commercial trade is supported. Fair Trade organisations do comply with a number of RBP criteria. Their emphasis on suppliers is evident, as would be expected, and this aspect in particular does challenge the mainstream about its own supply chain practices. Similarly, their focus on employees, communication with stakeholders and responsibility to the environment (all five respondents meeting these criteria) is further evidence of good practice. While Fair Trade organisations could and probably should do more to ensure compliance with general RBP criteria, the failings evident from this study do not suggest that their whole approach to the mainstream is currently undermined by their lack of attention to such criteria.

Conclusions

We have derived from the literature a set of 16 criteria for RBP in SMEs grouped into four categories (governance of RBP; employees in the organisation; stakeholder relationships; external reporting and monitoring). Fourteen of the 16 RBP criteria were found to be satisfied in at least one of the sample organisations. The two exceptions – the presence of an ethics committee and ethics training for employees – have reasonable explanations as to why, in U.K. Fair Trade organisations, they might not be satisfied. Hence, it seems reasonable to conclude that these 16 criteria should form the basis for further research. Such research, across a broader and international range of SMEs, including those outside the Fair Trade movement, might help to confirm or improve upon these 16 criteria and to assess whether the 57.5% 'satisfaction' rating for the five respondent organisations is common in other groups of SMEs. Further research may also identify similarities or disparities in RBP practice in relation to independence, size and age, and may provide evidence across sectors and in other geographic regions.

In relation to the Fair Trade organisations, development of their websites in relation to RBP criteria to more accurately reflect actual practice would seem to be a desirable action, together with some action on other RBP criteria where practice is currently lacking. This needs to recognise, however, that for some of these organisations the resource available to do this is limited and the focus is quite rightly on practical action in relation to Fair Trade rather than on RBP activities in general. Nonetheless, with the broader objective of Fair Trade being to influence the mainstream, such RBP disclosure and practice might be seen to be part of what a Fair Trade organisation should be doing. However, there is insufficient evidence here to suggest that currently Fair Trade's ability to influence the mainstream is undermined by deficiencies in such practice.

Finally, the study reported here was intended only as exploratory within the U.K. in order to assess the appropriateness of the 16 RBP criteria. In relation to Fair Trade, this study could be extended to all trading organisations in the IFAT fold. IFAT has already been presented with the report and recommendations that were provided to the organisations that responded to the request for further information, and so is already in a position to recommend action to its members. The extension of this initial exploratory study to such a large, international and multi-lingual population would potentially provide a rich, comparative set of data from which more general conclusions could be drawn.

Notes

[1] It is interesting to note that the European Parliament resolution on corporate social responsibility ''believes that the Commission should also consider establishing a list of criteria for enterprises to respect if they claim to be responsible'' (European Parliament, 2007, p. 3).

[2] Micro-businesses are defined as less than 10 employees, small as between 10 and 50 and medium as between 50 and 250 – see, for example, European Commission (2003, p. 28).

[3] FINE is an informal network that involves the Fairtrade Labelling Organizations International (FLO), the International Federation for Alternative Trade (IFAT), the Network of European Shops (NEWS!) and the European Fair Trade Association (EFTA).

[4] The brands above the Fair Trade organisations were, in rank order, the Co-op, Body Shop, Marks and Spencer, Ecover and Green and Blacks. See http://www.gfknop.com/imperia/md/content/gfk_nop/coes/brandstrategy/ethical_brands_top_level_findings_may08.pdf, accessed 26 September 2008.

[5] FLO currently sets standards for the following products: bananas, cocoa, coffee, dried fruit, fresh fruit and fresh vegetables, fruit juices, herbs and spices, honey, nuts and oil seeds, quince, rice, cane sugar, tea, wine grapes, flowers and plants, seed cotton and sports balls – www.fairtrade.net/standards.html, accessed 26 September 2008.

[6] IFAT has since added a tenth criterion: ''Trade Relations: The organization trades with concern for the social, economic and environmental well-being of marginalized small producers and does not maximise profit

at their expense. It is responsible and professional in meeting its commitments in a timely manner. Suppliers respect contracts and deliver products on time and to the desired quality and specifications. Producers and suppliers are paid in a timely manner and in line with agreements made. Whenever possible and if help is required, producers are assisted with access to pre-harvest or pre-production financing (advance payments). Buyers consult with suppliers before cancelling or rejecting orders. Where orders are cancelled through no fault of producers or suppliers, adequate compensation is guaranteed for work already done. The organization maintains long-term relationships based on solidarity, trust and mutual respect that contribute to the promotion and growth of fair trade. It maintains effective communication with its trading partners. Parties involved in a trading relationship seek to increase the volume of the trade between them and the value and diversity of their product offer as a means of growing fair trade for the producers. Buyers support processes which add value for producers in order to increase their incomes. The organization works cooperatively with other FTOs in country and avoids unfair competition. It avoids duplicating the designs or patterns of other organizations without permission'' (IFAT, 2008).

[7] Conversation with Marietta Shimizu-Larenas, Assistant Director of IFAT, during a visit to the IFAT offices, 26 June 2006.

[8] Five non-trading organisations also had IFAT membership: The British Association for Fair Trade Shops (BAFTS); Oxfam GB; Oxfam Ireland/Northern Ireland; The Body Shop Foundation and Traidcraft Exchange. The membership changes so that, for example, Tearcraft and Twin Trading were not included at the time of accessing the website (November 2005), despite being long-standing Fair Trade organisations and being on the website when the initial parameters of the research were being discussed. These two organisations do now appear again (www.ifat.org, accessed 26 September 2008).

Appendix 1

IFAT standards

	Standard	Description
1	Creating opportunities for economically disadvantaged producers	The organisation supports economically disadvantaged or marginalised producers. It seeks to enable them to move from a position of vulnerability to one of security and from material poverty to income and ownership
2	Transparency and accountability	The organisation is transparent in its management and commercial relations and deals fairly and respectfully with its trading partners It is accountable to all its stakeholders The organisation finds appropriate, participatory ways to involve employees/staff and producers in its decision-making processes and gives special attention to the dissemination of relevant information to all its trading partners
3	Capacity building	The organisation seeks to develop producers' skills … and commits to providing continuity in its trading relationships with its partners in the supply chain over an agreed given period The organisation also develops the skills of its own employees/staff
4	Promoting Fair Trade	The organisation raises awareness of the aim of Fair Trade and of the possibility for greater justice in world trade through Fair Trade It acknowledges the importance of customers for the growth and effectives of its movement. Customers are provided with information about the organisations, the products and in what conditions they are made. Honest advertising and marketing techniques are used. The organisation aims for the highest standards in product quality and packing

APPENDIX

continued

	Standard	Description
5	Payment of a fair price	A fair price is one that has been mutually agreed by all through dialogue and participation, which provides fair pay to the producers and can also be sustained by the market Fair Trade buyers, importers and intermediaries ensure prompt payment to their producers and other partners
6	Gender equity	The organisation provides opportunities for women and men to develop their skills and actively promotes applications from women for job vacancies. Women employees are provided with leadership training and encouraged to seek leadership roles Organisations working directly with producers ensure women's work is properly valued and rewarded. Women participate in decisions concerning the use of benefits accruing from the production process Local cultures and traditions are respected and steps taken to avoid discrimination on the grounds of religion, disability, caste or age
7	Working conditions	The organisation is taking steps to promote a safe and healthy working environment for producers. Working hours are in line with the conditions established by the law and ILO convention
8	Child labour	The organisation and its members respect the UN Convention on the Rights of the Child as well as the law and social norms in the local context
9	Environment	The organisation maximises the use of raw materials from sustainably managed sources buying locally when possible Recycled or easily biodegradable materials are used for packing and goods are dispatched by sea wherever possible The organisation promotes the use of technology that respects the environment as well as the use of initiatives to reduce energy consumption, and creates awareness of environmental hazards

Source: Adapted from IFAT Standards (2005).

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Social and Environmental Narrative Reporting
Analysts' Perceptions

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An ACCA research report, *Narrative Reporting: Analysts' Perceptions of its Value and Relevance* was published in November 2008. The research considered analysts' views on five key elements of narrative reporting, including social and environmental disclosures.

Due to the significant interests ACCA has in corporate transparency with regards to sustainability, this specific part of the research has been highlighted in this paper. The other parts of the research have been summarised only.

The full report has been published as ACCA research report no. 104, *Narrative Reporting: Analysts' Perceptions of its Value and Relevance,* by Dr David Campbell, senior lecturer in accounting, Newcastle University and Richard Slack, reader in accounting, Newcastle Business School, Northumbria University.

The report is available free of charge, in PDF from www.accaglobal.com/research
or as hard copy from connect.orders@accaglobal.com

Introduction

THE INFORMATION 'SUPPLY CHAIN'

The passage of information from reporters to consumers of corporate information is a complex one but an approximate 'supply chain' can be identified, at least as far as institutional stock market participants are concerned.

The reporting company makes disclosure through a number of media. These will typically include analysts' briefings at the time of the publication of the results, interim accounts, final annual report and accounts (usually several weeks after the initial analysts' briefings), 'stand alone' reports and press statements made to the press or through the investor relations department. Most of the financial information used by analysts is made available at the results publication date, some weeks ahead (usually) of the publication of the annual report. The annual report is mainly used, where it is used at all, for its narrative content and small items of financial information, not in the preliminary results (such as board members' salaries).

Based on their reading of a company's financial and other strategic information, sell-side analysts provide advice to buy-side clients. The formal channel for this is the analysts' report, produced to an approximate pro forma.

Publication is commonly through subscription-based online sources that are available to the buy-side, although informal contact also takes place where more robust views on individual stocks might be exchanged. The analyst's report, as a document in the public domain, tends to be carefully worded. In the event that 'coded' statements are not understood by favoured buy-side clients, the informal contact conveys enriching information over and above the formal report.

Sell-side analysts are a key part of the information 'supply chain', and the basis for the primary research undertaken for this report. The buy-side makes use of a number of sources of information but tends to rely quite heavily on sell-side analysts' reports.

The buy-side will typically receive several analysts' reports, through the online subscription provider, on any given sector or stock. The buy-side will typically look for 'snippets' of research 'over and above' the template or pro forma. Advice based on experiences beyond the financial information is valued, although because of the politics of the relationship between analyst and company this is often difficult to provide.

THE CHANGING ROLE AND CONTENT OF THE ANNUAL REPORT

Annual reports have grown in length over the recent decades. The general expansion of explanatory notes to the accounts, and the requirements under different corporate governance code provisions for more information, have been accompanied by some additional requirements under recent companies acts and listing rules. Annual reports have been noteworthy more recently because of the increased amount of narrative reporting. This is thought to be related to the increased public scrutiny of business activities and the assumed need to explain various aspects of activity not amenable to numerical conveyance.

Whereas, at one time, the annual report would be the only public document produced by companies, the changing landscape of corporate communications has reinforced the importance of questions on why the annual report is a suitable vehicle for some narrative disclosures. In addition to stand alone social and environmental reports, it is likely that the company website has become the vehicle of choice for most stakeholders seeking information on a company.

Methodology

RESEARCH QUESTIONS

Analysts were asked about five specific 'categories' of voluntary disclosure of narrative reporting, with the aim to identify the materiality and usefulness of such narrative disclosures to sell-side analysts. The 'categories' were:

- the importance of narrative reporting
- the chairman's statement and strategy reporting
- risk disclosures
- corporate governance disclosures
- social and environmental disclosures.

This short paper summarises the findings of the first four elements, but presents a fuller report on the findings of social and environmental disclosures. The full report can be viewed at www.accaglobal.com/research

In total, 19 sell-side banking analysts were interviewed from one sector. This single sectoral representation enabled intra-industry observations to be made. Second, it enabled the information needs of one particular cohort of sectoral analysts to be examined in detail.

The study focused attention on the analysts of UK banks for two reasons. First, it facilitated the interrogation of the perspectives and views of a high proportion of the London-based analysts of a strategically important sector for the UK and European economy. Second, there are ample reasons why all of the narrative disclosures under consideration in this research could be material and/or useful to investors.

METHOD

In order to identify a cohort of analysts to approach, the list of analysts that covered Alliance & Leicester plc was used as a starting point. The interviews took place at the London office of each analyst between the autumn of 2004 and the summer of 2006. The final number of suitable analysts interviewed for the project was 19.

At the start of each interview, the analyst was initially assured that his or her responses would be fully anonymised. After that, Alliance & Leicester plc's annual report and accounts for year-end 2003 was produced by the interviewer and the analyst was invited to describe how he or she would use the document if that was the first time they had seen it. This report was used for two reasons: first, it contained examples of all of the categories of narrative disclosure being studied; and second, it was more manageable in size in comparison to reports from some other banks.

The cohort of analysts interviewed for this research had an average of eight and a half years' experience in the job. The majority were not professionally qualified in accounting although all were qualified to degree level or higher. The most common academic backgrounds of interviewees were (in order) economics, maths, finance, accounting and law.

Evidence from analysts

OVERALL VIEWS ON THE ANNUAL REPORT

Almost all of the analysts interviewed discussed the limitations of the annual report in terms of the timing of its publication. While the year-end results are accompanied by the preliminary accounts, the final printed version of the annual report and accounts is often not published until some weeks later, by which time the information in the prelims has formed the basis of the analysts' forecasts. This publication lag significantly reduces the usefulness of the final document as an investment-material source of information. The detail in the preliminaries and the information conveyed by management at the results presentation are far more important in the intervening period.

Analyst A2 noted: 'On the basis that you get your report and accounts after you've already had the preliminary results, you are two months down the line from when you were actually given the specific… information in the preliminary results.'

The majority of the analysts referred to the document as potentially important for new information that is most likely to be in the detail and, possibly, in the notes to the accounts. In this regard, it is used as a historical document that contains more detail than the preliminaries. There was also criticism concerning the increased length and complexity of annual reports.

The contents of the annual report in general were considered by most to be potentially very relevant to the investment decision, although the cohort differed substantially in the use they made of the document.

One of the prominent emphases made by all of the analysts in the sample was the overwhelming importance placed upon the numerical financial data in annual reports. This was not an unexpected finding in that one of the main roles of an analyst is to forecast the key financial statistics over the forthcoming period and the recent history of those statistics is, therefore, of utmost interest.

The order of where the cohort referred to first in the annual report varied but, in almost all cases, the first 'port of call' was either the income statement or the notes to the accounts. The balance sheet was considered less important in most situations than the income statement and the cash flow statement was generally viewed as less material again.

A general scepticism with which reported figures were viewed was expressed by most of the cohort. Financial ratios given by the reporting company were never taken at 'face value', and other figures were frequently added back to reported costs and earnings, to arrive at what the analysts considered a more reliable figure.

THE IMPORTANCE OF NARRATIVE REPORTING

It was while discussing the annual report content outside the financials that differences of opinions between analysts became evident. This is the section of the annual report that has seen the most growth over recent years. In this context, 'front end' includes the collective disclosures that take narrative rather then numerical form. This section of the annual report would theoretically be of interest when the information sought is not available – or cannot be expressed by – the financial information. In practice, much of what is in the narrative sections is content already seen in the preliminaries, so it suffers from the same time lag limitation as other content of the annual report as a whole.

The cohort of analysts expressed mixed opinions on the materiality and usefulness of 'front end' narrative reporting. Despite misgivings, however, the consensus overall view was that the 'front end' was capable of containing content of material use to analysts, such as a statements about the management and monitoring of targets.

THE CHAIRMAN'S STATEMENT

There is no prescription in company law nor listing rules as to the content of the chairman's statement. In practice, chairmen have typically used the statement (or 'letter') as a vehicle for summarising the previous year's performance, to highlight any key changes, to acknowledge those who have contributed to any successes and to comment on 'going concern' and future prospect issues over the subsequent year.

There was a considerable and prevailing expression of scepticism over the value of the content. Analyst A13 provided a helpful summary of the way in which most analysts view the chairman's statement. 'I've yet to read one that tells us anything that we either weren't told at an analysts' meeting two months before the financials came out or that isn't part of a communicated strategy that's been around for ages.'

The most usual reason for the dismissal of the chairman's statement as a material and useful disclosure was its lack of detail and its cursory treatment of information on the company's strategy.

RISK DISCLOSURE

Risk disclosure and risk management information is one of the most notable additions to the voluntary content of annual reports in recent years.

The majority of analysts expressed scepticism about narrative risk reporting in the annual report. A typical opinion was that risk reporting was simply a 'boiler-plating' or a 'tick-box' exercise performed annually by companies without any real attempt to report on the actual changes in risk exposure over the year nor as anticipated in the year ahead. Most of the analysts relied on their own sector relevant knowledge of banking risks and risk management, and viewed disclosure as being, for the most part, meaningless to them. Moreover, the levels of disclosure were often regarded as being too simplistic for analysts on the one hand, but perhaps too complex for the individual non-specialist investor on the other. In this respect, it was suggested that risk reporting failed as a material disclosure for both types of annual report user.

Referring to the risk narrative, Analyst A5 said, 'that's generic what's written there and it's probably not even a very good description of [risk] to someone who didn't really understand [such as an independent investor]. Does it really tell you anything? No.'

There was, nevertheless, a general feeling that the presence of risk narrative was a potential source of comfort to analysts, even though the content was probably not of direct material interest. Only one analyst (Analyst A1) in the cohort of 19 expressed something approximating to a positive view of the current state of risk reporting.

CORPORATE GOVERNANCE DISCLOSURE

In the UK, corporate governance code compliance is voluntary in law but effectively mandatory under stock market listing rules. Companies can technically 'comply or explain', but in practice, large companies, and especially banks, normally comply in full to maximise market confidence. One of the results of the increased raft of corporate governance codes in recent years has been a substantial volumetric increase in corporate governance reporting.

With regard to reporting, the prevailing view was that while the presence of corporate governance content was important, it was of little materiality or use to the cohort of analysts. Others expressed blunter opinions, saying that they didn't read the corporate governance content at all.

“...absolutely useless
from my point of view.”

“...don’t give a damn.
Personally I might give a damn.
Professionally I don’t care.”

“...very laudable
but I’m not interested.”

“...speaking purely from an
investment analyst perspective,
it’s not useful at all...”

Social and environmental disclosure

There has been relatively little by way of interrogation of a user cohort as to the usefulness and materiality of social, environmental and ethical (SE) reporting. The evidence offered by the analysts in this study suggests a range of responses to this reporting category but with the prevailing belief that both social and environmental matters are of limited interest to the professional analyst and forecaster. In organising the evidence in this disclosure category, content is set out in five subsections, discussing:

- whether SE narrative is used and its materiality
- evidence that some analysts may misunderstand the nature of SE narrative
- environmental risk and disclosure
- the potential (rather then the current) materiality of SE reporting
- the way in which SE reporting is seen in the context of the whole annual report.

USE MADE, AND MATERIALITY OF, SE NARRATIVE REPORTING

Analyst A2 put the issue in some kind of context, saying, 'as I say banks, although they do have a part in the social fabric and so on…the whole kind of stakeholder idea – for what I'm trying to do [social and environmental reporting is] not that relevant really.' Analyst A15, as part of a commentary on his or her use of annual report contents said, 'corporate social responsibility report? Even more useless [than the chairman's statement and corporate governance].' Analyst A17 said, 'it sounds bad but from our point of view at the moment this CSR/environmental [disclosure] is close to useless.'

Upon probing in a little depth, it became apparent that social and environmental reporting was, for the cohort of analysts, perhaps the least read and least relevant part of the entire annual report. Analyst A1 was asked 'Are you interested in social and environmental disclosure at all?' which received the reply, 'Not really, no.' Analyst A2 said, 'Frankly I'd ignore it really' and Analyst A4 said that 'Corporate and social [disclosure was] definitely no use.' Analyst A7 reported that it was 'absolutely useless from my point of view.'

Analyst A1 confessed that, 'I've never really looked at one [a social and environmental report] before so I could be just alone [in my view, but] we've got so many pressures on our time that it's quite low in our list of priorities to actually read through that and if you've got to read the whole report that's going to be the last [thing you would read].'

Analyst A6 said that he or she would read the social and environmental report, 'very, very rarely…actually I don't think I've ever read through one.' Analyst A10 said of social and environmental reporting, 'don't give a damn. Personally I might give a damn. Professionally I don't care.' Analyst A11 said, 'very laudable but I'm not interested,' Analyst A13's view was that 'speaking purely from an investment analyst perspective it's not useful at all,' and Analyst A12 said 'I don't read that part of the account.'

Similarly, Analyst A16 said, 'I can't see any value in that section. I've probably never read one.' Analyst A4 had been dismissive about the rest of the business ethics reporting and was, similarly, dismissive with regard to environmental disclosure. 'Environmental blah blah blah. It's a bank,' implying that this identity this had a bearing on its interest in environmental matters. Analyst A13 said that environmental narrative was 'even less useful' than the social and ethical components. Analyst A14's view was, 'I think…it's a waste of money to be printing a lot of this and also I suppose there's a kind of irony in printing an environmental report that nobody reads.'

“I can’t see any value in that section.
I’ve probably never read one”

“These are more soft issues and they wouldn’t be driving the [forecasting] model.”

“I’m not convinced that, at the moment, those sorts of considerations [such as] CSR disclosures, drive share prices.”

With specific regard to social and environmental narrative and the question of materiality, the consensus view was that it was perhaps the least material (actual or potential) component of the annual report. There were, according to the cohort, a small number of situations in which it could be material to investment decisions but these were considered to be marginal: analysing for socially responsible funds or when a specific environmental risk applies. Analyst A6 reported that, 'if the client's funds aren't socially responsible… then this sort of stuff is obviously somewhat less relevant to an extent from that [materiality] point of view.'

Analyst A5 was asked: 'So in terms of your work as an analyst how you would judge the CSR component [of the annual report]?' Analyst A5 responded: 'Not material at all. There might be analysts out there who sit and read this from cover to cover but is there anything in here material that's going to affect the share price? No.'

Analyst A9 highlighted a limitation of all narrative reporting, to analysts, with specific reference to social and environmental content, saying that, 'These are more soft issues and they wouldn't be driving the [forecasting] model. We are about numbers. We are putting numbers in a spreadsheet and coming up with a forecast.' The implication of this comment is that unlike some other narratives, social and environmental reporting is unlikely to contain information capable of amending or informing any aspect of the financial forecasting model. In this respect, it seems there is a weak belief that any important environmental risks would be discussed in the social and environmental narrative.

Analyst A12 expanded on this belief. 'I know that there is an increasing demand in the market for ethical investment and those sorts of disclosures can help convince people of the ethics of investing in companies but we're really interested in financial performance and valuation. I'm not convinced that at the moment those sorts of considerations [such as] CSR disclosures drive share prices.'

Analyst A18 expressed a similar view. 'I wouldn't say they were completely useless but nothing from those sections go into our models on how the companies work. We never write about that section at all.'

MISUNDERSTANDING OF SE REPORTING

A small amount of evidence emerged that analysts may, in their unwillingness to (in some cases) read the social and environmental section of an annual report, have misunderstood its content. Analyst A4, for example, was dismissive, saying: 'Looking at it, its just sort of for customers who are deaf, hard of hearing or have speech impediments, a fully qualified sign language interpreter is available on request.' Analyst A14 was seemingly unaware of the more detailed content of social and environmental reporting that has been introduced in recent years. 'I don't think that corporate social responsibility has any bearing on socially responsible investor issues because its all about how much paper – well I'm guessing because I haven't read one – but I'm guessing its all about how much paper they've used and all this kind of stuff. Terribly irrelevant.'

ENVIRONMENTAL DISCLOSURE AND SECONDARY ENVIRONMENTAL RISK

One of the particular issues that the researchers wanted to explore with the cohort was the importance placed on banks' environmental exposure through its loan book rather than through its direct operations. Analyst A3 was asked about the general environmental risks for a bank. The interviewer added, 'You wouldn't see environmental risk as part of the risk of the business at all?' The answer was typical of those failing to recognise indirect environmental risk. 'Not really in a bank. Certainly if it was like a nuclear power station or an oil company I might worry about it a bit more'.

“...it may be nice to think about the environment a bit on the side but I don't like to inlay that decision into my pension pot.”

Which section is the least material to you?

“it would probably be the environmental report.”

“it wouldn't affect me if you lost the whole corporate responsibility section really.”

Analyst A9 gave a blunt answer to the question of whether he or she would ever consider that banks might be complicit in pollution or expose themselves to environmental risks by their lending decisions, saying, 'No. Straightforward answer. No.'

Analyst A17 expressed similar misgivings, saying: 'If banks by their lending can be held accountable for what the company does with the loan that would make it close to impossible for banks to do anything. The environmental impact, just doing the actual report they would have to use half an entire rain forest just to publish the report'.

Analyst A18's view was that it was not the bank's purpose to moderate lending activity using environmental criteria. 'I think, to be honest, that is the government's job to regulate what industry does and I think ultimately the management of any company should try and maximise shareholder value.'

Analyst A13 was asked whether he or she could ever envisage a situation where the environmental exposure from the loan book would ever be material to an analyst's forecasts. 'From my perspective, and certainly given the tasks I have, I can't imagine it ever being material.'

POTENTIAL MATERIALITY OF SE DISCLOSURE

Given the responses from the cohort on their views on the current relevance and materiality of social and environmental narratives, follow-up questions were asked on the situations that may increase their materiality in the future.

The size of the change needed was highlighted by Analyst A3 who was asked: 'Could you ever see a situation where an environmental disclosure or a community disclosure would ever be material disclosure for you as an analyst?'

'Yes I could. It would purely be if it was driven by my clients – if we end up with a huge socially responsible investment community that dominates the landscape. At the moment the sort of people like you and I invest in our pensions wanting to have a safe retirement, it may be nice to think about the environment a bit on the side but I don't like to inlay that decision into my pension pot'.

Analyst A12 expressed two viewpoints. 'Well the way things are going ethical investing is really taking off' and continued by saying, 'That's a growing phenomenon so there are people in the market that are focusing on these things and if interest in those sorts of issues carries on growing at the rate that it has been then yes I can, in the future, conceive of a time when these sorts of things will be material.'

In concluding, however, Analyst A12 said, 'but we're actually a long way off from that now.'

LEAST MATERIAL PART OF AN ANNUAL REPORT

Given the general scepticism of the value of the SE narrative in banks' annual reports, each analyst was invited to nominate a section that was the 'least material' to him or her in the conduct of their jobs as analysts.

Analyst A1 spoke for the majority, by saying, 'for me as an analyst it would probably be the environmental report.'

With a note of sarcasm, Analyst A11 said, 'I'll shock you by saying the corporate social responsibility report.' Some analysts discussed a situation in which the SE content was not present in the annual report at all.

Analyst A14 said, 'No I wouldn't miss it. It would greatly facilitate my reading of the rest of it because it wouldn't be in the way,' and continued to note that it was a section that, 'nobody reads.' Analyst A16 said that, 'It will sound awful but it wouldn't affect me if you lost the whole corporate responsibility section really.'

Discussion

ISSUES FOR PREPARERS

It is curious, given the substantial growth in narrative content over the years, that little systematic evidence exists for the actual manner in which corporate reporting information is consumed. While a part of the volumetric increase can be explained in terms in increased regulation and stock market listing requirements, it remains the case that the vast bulk of the increase is due to enhanced voluntary narrative. Reporters have bulked out their annual reports with more and more content, but little is known as to which audiences consume the respective parts of the annual report nor the actual or potential investment materialities of those components.

This study has found that at a fundamental level, the narrative contents of annual reports are relatively unimportant to analysts who are one of the most important primary consumers of corporate reporting information. There was no consensus among the cohort that any given narrative content category was actually, or even potentially, material and the majority view was that each section was less than useful. Some sections of narrative reporting were seen by the analysts as being of almost no actual or potential materiality at all.

The most common reasons given by analysts for the assumed immateriality of the relevant disclosures were the lack of numerical content, lack of granularity or the assumption that their own clients (the buy-side) weren't interested in information based on the type of voluntary narrative in question. So who is all this extra disclosure content actually for? Which audiences are conceived of when the content is being drafted? Some narrative sections were especially poorly thought of by the cohort of analysts. There were very few positive views on the chairman's statement while the risk narrative was considered largely 'boiler-plating' and the social and environmental content was universally considered irrelevant. A challenge appears to exist for reporters to take their readers' information needs into greater account when preparing for and drafting annual reports.

ISSUES FOR CHANGE AND ANALYSTS' INSIGHT

Evidence from this study suggests that analysts are very systems-driven and do not often think beyond the narrow confines of their roles in the capital market information 'supply chain'. It appears unlikely that they would be a source of pressure for change in terms of the social or environmental performance of businesses they cover as analysts.

They do, however, claim to be sensitive to the information needs of their own clients in the information supply chain. In this respect, it appears that pressure from the buy-side on such issues as environmental performance may cause a sell-side reappraisal of the materiality and value on social and, particularly, environmental reporting. It may be that investor pressure on the buy-side for, say, filtration by environmental risk, performance or reporting will present pressure for change in the environmental awareness of analysts. Internal change among the sell-side analysts themselves is unlikely though. The assumptions of capitalism pertaining to the supremacy of short-term growth and returns pervade the analysts' operational activity.

There may be some grounds for questioning the structural appropriateness of the analysts' skill set in interpreting narrative material for the purposes of financial planning and in respect of the failure to recognise the potential materiality of secondary environmental risk. The analysts were quick to dismiss narrative reporting as immaterial owing to its inability to be fed into a forecasting model, but a case could be made that, notwithstanding the perfunctory nature of much narrative reporting, it is the role of the analyst to interpret narrative content for the purposes of amending numerical forecasting.

The unwillingness to recognise the possibility of secondary environmental risk may be symptomatic of the short termism of analysts' financial forecasts.

TECH-TP-SEN

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Narrative Reporting: Analysts' Perceptions of its Value and Relevance

Narrative Reporting: Analysts' Perceptions of its Value and Relevance

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Contents

Glossary

Buy-side	Consumers of analysts' reports (including narrative and forecast data) such as fund managers.
Corporate governance reporting	Annual report disclosure containing information relating to corporate governance and reported compliance with corporate governance codes. Sometimes of interest because it contains details of directors' rewards.
Equities	Issued share capital of public companies traded on the equities markets (London Stock Exchange, etc.)
Equity research	Production of forecast information by sell-side analysts primarily cashflow and profit based measures, and management strategy to support buy/sell/hold recommendations and reports on equities.
Forecasting	Future profit and loss, cashflow and balance sheet predictions based on current available accounting information and management comment.
Front end	Annual report sections devoted to voluntary disclosure narrative prior to statutory reporting sections typically starting with the directors' report.
Fund managers	Individuals within investment companies, assurance and pension funds responsible for equity, debt, cash and other financial instrument allocation and selection within funds under their management (managed funds).
Information 'supply chain'	The process of production of accounting information (by preparer companies), its interpretation (by sell-side analysts) and its consumption (by buy-side). The consumption and use of accounting and other annual report information from companies used by sell-side analysts for their equity reports and recommendations to buy-side funds.
Mandatory/statutory disclosure	Reporting compliant with relevant reporting standards and regulatory/legislative instruments.
Preparers	Public companies that publish reporting data compliant with relevant IFRS and legislative frameworks. Annual reports also include voluntary narrative disclosure.
Risk reporting	Voluntary reporting relating to risks that companies are exposed such as financial and operating risks and their management of those risks.
Sell-side	Producers of equities research and forecasting data for consumption by fund managers and other buy side participants.
Social and environmental reporting	Voluntary disclosure containing information on the company's impacts upon a range of social and environmental constituencies or stakeholders. Typical contents include information on human resources, communities, environmental resource consumption and environmental impact.
Strategy reporting	Information containing detail on the company's strategy. Typically forward looking in tone, it is more likely to be present in the chairman's statement or the chief executive's statement in an annual report.
Voluntary disclosure/ narrative	Information provided by companies within annual reports not covered by statutory reporting requirements including social, environmental and risk disclo sures

Executive summary

‘Analysts like numbers, to be honest’

ANALYST A9

INTRODUCTION TO THE TOPIC

This research report is about the voluntary narrative sections of company annual reports, with particular reference to the annual reports of UK banks. Voluntary narratives are defined as those parts of the annual report not mandated by Companies Act requirements and not reported on as part of the audit report. Such disclosure narratives include, among other things, the chairman’s statement, chief executive’s review, social and environmental reports, and risk disclosures. There is an academic literature that has examined the patterns of voluntary disclosure and these contributions have fallen roughly into three general categories: empirical studies examining trends and changes in reporting; theory building and testing contributions; and user-needs analyses. It is to this latter strand of literature that this study aims to make a contribution.

There has been a marked growth in many types of voluntary and narrative reporting in recent years, with media other than the hard copy annual reports in the ascendant as carriers of reporting messages. Despite this growth, large companies continue to produce elaborate, lengthy and detailed annual reports with narrative sections extending to, in some cases, hundreds of pages. The annual reports for 2006 of HSBC Holdings plc and Barclays plc were 458 pages and 310 pages respectively.

One of the questions frequently raised, but not well answered, in considering this growth is the actual usefulness of this surfeit of narrative in annual reports. Who reads it, is the information useful and is it material to fund allocation decisions made by investors? And if not, what are the implications for preparers of annual reports?

AIMS AND OBJECTIVES OF THE RESEARCH

The primary aim of this research is to explore questions of usefulness and materiality of annual report narrative disclosures. The research addresses calls made by, among others, Smith (2004: 202), who suggests that, ‘future research will more widely examine the discretionary disclosures made by firms to explore their impact on decision makers and on investment analysts’ stock recommendations’. In order to do this, a method was chosen that would facilitate an in-depth and narrative-rich discussion of the issues in question with perhaps the single most important and influential user group of audited and narrative company reporting: sell-side analysts.

The sell-side’s role as the primary interpreter of company information for buy-side and fund management purposes makes it a suitable source of opinion on the research question, as it is the sell-side’s consumption of corporate reporting upon which fund allocation decisions are ultimately made. Given that, in volume terms, most institutional ‘real money’ changes hands on the basis of sell-side advice, sell-side analysts are uniquely placed to comment on the investment materiality of a range of voluntary narratives and it was upon that basis that they were selected for this study.

Nineteen London-based sell-side analysts were interviewed between late 2004 and mid 2006, each of whom analysed only the banking sector. The focus on the banking sector was for several reasons, prominent among which was the fact that banking (along with technology, pharmaceutical and oil/gas) is one of the four main ‘volume’ trading sectors in London, strategically important to the UK economy and comprising approximately 15% of the total FTSE 100 market value. It was further believed that focusing on one sector rather than performing a shallower cross-sectional study would enable a greater penetration to be made of issues relevant to materiality in that single sector. All analysts were interviewed using a semi-formal method, and interview transcriptions were content analysed and sorted by the category of voluntary disclosure being discussed.

SUMMARY OF FINDINGS

Each analyst expressed views on a range of voluntary and narrative disclosure categories, including management commentaries such as the chairman's statement, chief executive's review, operating and financial review, risk reporting and the corporate governance statement. In addition, other areas of voluntary narrative were discussed at some length including social, environmental and ethical reporting (partly because these issues have preoccupied many academic researchers in the field).

There was a general belief that narrative reporting was not immediately applicable nor helpful in the primary tasks of the sell-side which is to construct forecast models and produce written reports for the buy-side. The normal view was that narrative reporting was less useful to analysts than to other putative users of annual reports but most analysts were unable to identify specific consumers of any given disclosure category.

The chairman's statement was generally considered to be less useful than the chief executive's review because the latter was more likely (in most annual reports) to contain meaningful information on future strategy. The content of the chairman's statement was generally dismissed as irrelevant to the investment decision or to any forecasting figure. Risk disclosure was generally thought of as too general in nature to be useful. Corporate governance reporting (mandatory under listing rules under UK 'comply or explain' practice) was usually unread because governance in UK banking was generally trusted by the analysts. Social and environmental reporting was universally considered irrelevant and incapable of influencing a financial forecast. It was rarely read by analysts and any suggestion that the environmental reporting might contain disclosures germane to the description of secondary (ie loan book) environmental risk was dismissed.

IMPLICATIONS OF FINDINGS

Analysts were shown by this research to be technocratic and rules-driven in nature, and unlikely to be a source of change in respect of social and environmental issues. They were generally sceptical about all voluntary narrative reporting and were dismissive of large sections of it as irrelevant, 'useless' or worse.

There are a number of issues raised by the findings. Prominently, these findings represent a challenge to preparers of annual reports, who have presided over a period of volumetric expansion of narrative content, the value of much of which to analysts can now be questioned. If it is the intention of preparers to make narrative reporting relevant and material to investors, they appear to have some way to go or some rethinking to do.

Similarly, however, the findings highlight the way in which analysts are dismissive of anything other than directly value-relevant numerical data. The belief that no narrative reporting is capable of informing, amending or challenging a financial forecast is a curious one.

1. Introduction

'You're never satisfied with what you're given. You always want more. That's it, end of story. You always want more. You always want the better description, you want more granularity, you want more information as an analyst to get a better understanding of what's going on in the business.'

ANALYST A5

There is a growing tradition of research in voluntary disclosure of accounting information. Several themes or genres of research can be identified in the literature with those prominent including descriptive studies, theory testing and user-needs analysis and perspectives. Descriptive studies are those that have noted changes and trends in various aspects of reporting behaviour; theory-testing studies are those that have attempted to use reporting evidence to inform a variety of theoretical perspectives; while user-perspective studies have sought to identify user needs and measure reporting against those needs. This study seeks to make a contribution to the last of these three genres.

1.1 THE INFORMATION 'SUPPLY CHAIN'

The passage of information from reporters to consumers of corporate information is a complex one but an approximate 'supply chain' can be identified, at least as far as institutional stock market participants are concerned. The situation is slightly different for some individual and smaller investors.

The reporting company makes disclosure through a number of media. These will typically include analysts' briefings at the time of the publication of the results, interim accounts, final annual report and accounts (usually several weeks after the initial analysts' briefings), 'stand alone' reports and press statements made to the press or through the investor relations department. Most of the financial information used by analysts is made available at the results publication date, some weeks ahead (usually) of the publication of the annual report, and the annual report is mainly used, where it is used at all, for its narrative content and small items of financial information not in the preliminary results (such as board members' salaries).

On the basis of their reading of a company's financials and other strategic information, sell-side analysts provide advice to buy-side clients. The formal channel for this is the analysts' report, produced to an approximate pro forma (although this may be disputed by some analysts) and it is common, although obviously not compulsory, for this to be shown to the subject company's investor relations department being analysed, prior to publication. The investor relations department may then suggest amendments before the report is published.

Publication is commonly through subscription-based online sources that are available to the buy-side although informal contact also takes place where more robust views on individual stocks might be exchanged. The analyst's report, as a document in the public domain, tends to be carefully worded. But in the event that 'coded' statements are not understood by favoured buy-side clients, the informal contact conveys enriching information over and above the formal report.

Sell-side analysts are a key part of the information 'supply chain', and the basis for the primary research undertaken for this report. Their importance in the 'supply chain' has been recognised in the academic literature. Johansson (2007: 30), for example, comments that: 'sell-side analysts are ... key actors in this market and the analysts' relations with company representatives and clients seem to be a central part of the value-creation chain in the market'. Jackson (2005) and Ljungqvist et al. (2007) also both recognise the primary role of the sell-side analyst acting as an information intermediary in the investment process. Lui et al. (2007: 630) say that: 'given that [sell-side] analysts have been shown to influence investor behaviour and given the importance of risk in making investment decisions, an empirical investigation of analysts' risk assessments seems long overdue. In general, analysts add value by both aggregating publicly available information and generating new information.' In the professional and practice media, Investor Relations Society (2003) commented that: 'sell-side analysts remain an important audience for corporate communications. Sell-side analysts still play an important role in the market'.

The buy-side makes use of a number of sources of information but tends to rely quite heavily on sell-side analysts' reports. Most investment houses impose restrictions on share dealing behaviour by fund managers that goes against the explicit advice of the sell-side. Because fund managers typically deal in many stocks at a time, they use direct company information only intermittently. Although a fund manager may read an annual report for a particularly important stock, this is not a systematic activity and so the sector- and company-specific information provided by the sell-side is seen as very important.

The polling organisation MORI conducted a survey for the Financial Services Authority in 2005 that involved 300 interviews with respondents at buy-side organisations. The initial question posed was: ‘How important would you say investment research produced by sell-side institutions is as a source of information and ideas about the companies, sectors or assets you follow or invest in?’ (FSA 2005: 20). The responses demonstrated the importance of the sell-side to the buy-side, with 29% viewing sell-side research as ‘very important’ and 52% as ‘important’. Only 14% of respondents viewed sell-side advice as ‘unimportant’.

Similarly, Ethical Corporation reports, ‘the role of sell-side analysts is seen as crucial, as their views are given weight not only by asset managers, but also by high-level managers in companies themselves’ (Schiller 2005). This practice-based research is consistent with the findings of Womack (1996) and, more recently, Johansson (2007) who examine the role of sell-side analysts in the information supply chain. Johansson (2007: 31) says that: ‘in a short time perspective, the analysts’ recommendations seem to influence the price of a stock, and, according to studies on the market level, their written recommendations tend to convey valuable and new information.’

The buy-side will typically receive several analysts’ reports, through the online subscription provider, on any given sector or stock. Over time, favoured analysts will be followed and less favoured ones will not. In each case, however, the buy-side will typically look for ‘snippets’ of research ‘over and above’ the template or pro forma. Advice based on experience beyond the financial information is valued, although because of the politics of the relationship between analyst and company this is often difficult to provide. This brings us, however, to the next section.

1.2 THE RELATIONSHIP BETWEEN COMPANIES AND ANALYSTS

In the information ‘supply chain’ then, the sell-side analyst is the primary interpreter of company reporting. Given that fund managers, who are the actuators of fund allocations, do not systematically study company information directly, there is a heavy reliance on analysts’ interpretations of company situations and financial performance forecasts.

There is a tension in an analyst’s role between independence from a company being analysed and his or her dependence on the company in terms of information provision and general relations. There are a number of reasons why analysts send their reports to the analysed company prior to publication. The most prominent reasons are relationship management and checking for accuracy. The investor relations departments may make suggestions but if the analyst feels the need to say something negative in the report he or she must balance the strength of the wording with the need to manage the relationship with the company over the longer term. It is thought that senior company officers have their ‘favourite’ and ‘most trusted’ analysts that, it is believed, are the most likely to receive communications and information confirmations at key times. Inasmuch as such information can be a source of competitive advantage for an analyst, the management of that relationship, over many years, is very important.

It is conceivable, therefore, that some information germane to investment decisions is expressed in less than direct terms and in terms capable of being overlooked or missed altogether. Such ‘soft-pedalling’ in the interests of relationship management may be a source of concern to some observers in respect of the independence of analysts.

One of the analysts in the study (Analyst A2), speaking anonymously, was robust in his/her description of the company–analyst relationship, describing it as ‘adversarial’.

> *Analysts and companies are adversarial. The role of the analyst is to act on behalf of the investor and the analyst must expect that the company is potentially going to mislead them and therefore you have to take whatever they say with a significant amount of salt and you have to be looking for signs where perhaps numbers that they are forced to report… do not match up to management statements or other numbers that they’ve published.*

It seems to be the case, then, that a balance exists between analysts’ need to cultivate long-term relationships with the companies they cover and the need to maintain a healthy detachment and scepticism. The possibility that companies may seek to ‘mislead’ investors places analysts in a very important position in the information supply chain, as it is they who must interpret and discover such behaviour on behalf of those further down the supply chain that depend on their advice. Such a situation is explicitly recognised by Ljungqvist et al. (2007: 421) who state that:

> *companies care about what the analyst has to say about their stocks and could take their investment banking business elsewhere if they are unhappy with the analyst’s opinion. Thus sell-side analysts who work for integrated investment banking houses could come under implicit (or occasionally explicit) pressure to publish more favorable* [sic] *research about their employers’ current or potential relationship clients to help boost investment banking fee revenue.*

This problem of the objectivity trade-off with relationship management and trade generation is discussed at length by Jackson (2005), Lin and McNichols (1998), Ljungqvist et al. (2007), and Michaely and Womack (1999).

The reciprocity between company and analyst was discussed by several interviewees in the cohort used in this study. Analyst A16 was asked whether he or she believed that company finance directors were concerned about what analysts said about them.

> *I think they do care because I think a lack of disclosure at some level effectively puts up their cost of capital. I think it's a genuine driver and they know it. Companies with the most open, best disclosure, everything else being equal, tend to see a higher rating and that's, I think, something you can start to show.*

1.3 THE CHANGING ROLE AND CONTENT OF THE ANNUAL REPORT

Much of the prior research in voluntary disclosure has taken place in the context of the corporate annual report. Although voluntary disclosure on a range of issues takes place through media, including advertising, public relations documents, websites, special reports, press statements and through informal channels, research has centred on the annual report for several reasons. These have included the notion that as the only statutory annual communication with shareholders, anything considered important enough to be said would be conveyed in that document. Given that the company has almost total editorial control over the narrative content of the annual report, it is assumed to be the representative medium of a company's overall reporting intent. Botosan (1997: 331) notes that, 'the annual report is generally considered to be one of the most important sources of corporate information' while Gray S. J. et al. (1995: 45) goes slightly further, suggesting that, 'the annual report is a significant element in the overall disclosure process, given that it is the most widely disseminated source of [company] information'.

Annual reports have grown in length over the past recent decades. Campbell et al. (2006) reports that the average length of an annual report rose from 37 pages in 1974 to 90 pages in 2000. As they have grown in length, content has been added in response to a number of supposed information demands from users. The general expansion of explanatory notes to the accounts and the requirements under different corporate governance code provisions for more information have been accompanied by some additional requirements under recent companies acts and listing rules. In addition to legal, regulatory and statutory content, however, annual reports have been noteworthy in recent years for the increased amount of narrative reporting, 'the importance of [which]... by listed companies is expected to increase in the future' (Beattie et al. 2004: 232). Increased narrative reporting is thought to be related to the increased public scrutiny of business activities and the assumed need to explain various aspects of activity not amenable to numerical conveyance. Beattie and Pratt (2002: 1) note that, 'the importance of narrative reporting in annual reports has significantly increased' while Clatworthy and Jones (2001: 311), similarly, find that, 'accounting narratives are becoming increasingly important in external financial reporting.'

Gray S. J. et al. (1995) highlight the importance of distinguishing between types of information in examining voluntary disclosures. The voluntary narrative reporting categories that have attracted the attention of academic researchers include:

- risk reporting (eg Cabedo and Tirado 2004; Linsley and Shrives 2005; Linsley and Shrives 2006; Schrand and Elliot 1998; Woods 2004)
- the content of the chairman's statement (eg Arnold and Moizer 1984; Day 1986; Rippington and Taffler 1995; Smith and Taffler 2000)
- a range of other content that can generally be regarded as social, environmental and/or ethical in nature (eg Beattie and Pratt 2002; Deegan and Gordon 1996; Deegan and Rankin 1999; Gray, R. H. et al. 1995; Miles et al. 2002; Milne and Chan 1999; Solomon and Solomon 2006).

Previous academic studies have taken the opportunity to examine some of the trends and changes in these narrative reporting categories (see for instance Gray R. H. et al. 1995; Lehman 2004) and some have attempted to theorise links between changing reporting practices and changes in society in general (see for instance Patten 1995, Deegan and Gordon 1996, Wilmshurst and Frost 2000; and O'Donovan 2002). While several such studies have been published, few of them have addressed the issues of the materiality or usefulness of the increased narrative disclosures. It is to this genre of literature that this research report is intended to contribute.

Although academic studies have examined patterns in these disclosures, relatively few have examined the manner in which they are used by capital market participants. The prominent studies relevant to this research are detailed in the following literature review. Although a number of studies have sought, with varying degrees of success, to interrogate the views of a range of capital market participants, this report is one of the first to gain systematic evidence directly from the sell-side.

The importance of this study is also underlined by the growth in other media for corporate reporting purposes. Whereas at one time the annual report would be the only public document produced by companies (except for those that produced advertisements and other marketing literature), the changing landscape of corporate communications has reinforced the importance of questions on why the annual report is a suitable vehicle for some narrative disclosures. In addition to stand-alone social and environmental reports (which have emerged over the past decade or so), it is likely that the company website has become the vehicle of choice for most stakeholders seeking information on a company.

2. Literature review

2.1 ANALYSTS IN PREVIOUS RESEARCH

The position of sell-side analysts in the information 'supply chain' between reporting companies and investors has made them a suitable subject for a number of previous studies. As a cohort, analysts have been thought to be capable of speaking on the materiality of information, owing to their assumed role as interpreters of accounting 'numbers' and strategic intent.

As they are sophisticated users of corporate disclosures of varying types, Day (1986: 295) refers to analysts as, 'perhaps the most informed and articulate user group.' Their role in the flow of intelligence in capital markets is referred to by Fogarty and Rogers (2005: 331) who comment that: 'financial analysts employed by securities firms play an important role in the capital markets. Most importantly, the reports that they produce are given great consequence by many market participants'. Similarly, Vergoossen (1993: 219) remarks, 'since many investment decisions are based on their findings...investment analysts play an important role in the capital markets'.

This study is specifically concerned with how analysts regard voluntary disclosure narrative in the annual report. The debate between information sources and materiality has been evident in the literature for some time. In early studies, Lee and Tweedie (1975) and Firth (1978) both note that the annual report is an important information source for investment decisions, but both these studies were published prior to the development of other information sources used by analysts today, such as online sources and stand-alone reports. In the 1980s, Arnold and Moizer (1984) examined methods used by UK analysts to appraise equities. They find that the most used parts of the annual report are used for such purposes, with the profit and loss, and the balance sheet being the most used statements. This is consistent with the findings of Lee and Tweedie (1981) although again, being studies of their time, voluntary disclosures are not addressed (see also Bouwman et al. 1987).

Research into analysts' use of different information sources is reflected in the literature. In addition to examining which parts of the annual report are used by analysts, some studies ask about the relative importance placed upon the annual report compared with other information sources. In practice, 'other' information sources usually refers to direct contact with the reporting companies themselves. Inasmuch as direct 'personal' meetings for the disclosure of new information are unauthorised, 'direct contact' in this context tends to refer to analysts' briefings, contact with the investor relations department or direct contact with senior officers for the purpose of clarification and explanation only. A more detailed discussion of the extant literature addressing analyst use of annual reports now follows.

Several studies find that direct contact is generally considered more important to analysts (in terms of company analysis) than the information contained in the annual report. Pike et al.'s (1993) is typical of the studies that find that personal contacts between analysts and corporate personnel are more important than the annual report. In most cases, however, analysts said that they placed the annual report second only to (ie immediately behind) direct contact in terms of the usefulness and materiality of its content (Chang and Most 1985). Barker (1998), similarly, finds that analysts attach less importance to the annual report compared with personal contact, results announcements and analyst presentations (by companies at the financial year end). The reason for this is that, 'the annual report doesn't satisfy analysts' short term news orientation' (Barker 1998: 12; see also Hellman 1996). A small number of other studies find responses at some variance to this 'order'. Brown (1997) finds the annual report to be the most important information source while Vergoossen (1993) finds that the majority of analysts rate, 'the most recent annual report as their most important source of information' (Vergoossen 1993: 229). Eccles and Mavrinac (1995) find, conversely, that the annual report is in third place behind direct contact and press reports in its importance as an information source.

Previous analyst studies that inquired about the section of annual reports of most use to analysts overwhelmingly find that the financials were the most used. Brown (1997) finds the income statement (profit and loss statement) to be the most useful annual report component. Chang and Most (1985) find the same in terms of the importance of the income statement and also find that the balance sheet and notes to the accounts are the next most important components. They go on to report that front end parts (such as narrative sections) are considered the least important, with the supervisory board report (directors' report in the UK) being noted as particularly insignificant. Previtts et al. (1994) note that sell-side analysts find the income statement and cash flow statements to be of most use, followed by segmental information by geographic area/business unit. They find that the usefulness of non-financial (narrative) information centres on quality of management, new developments and other changes. Other studies examining analyst behaviour in respect of voluntary reporting include Anderson and Potter (1998); Biggs (1984); Birts et al. (1997); Bouwman (1984); Bouwman et al. (1987); Flostrand and Strom (2006); Gray and Skogsvik (2004); Rogers and Grant (1997); Snyder (1999).

Flostrand and Strom (2006) compare 200 analyst reports to 200 matched annual reports to examine the relevance of non-financial disclosure and the use made of such disclosure by analysts in their company valuation process. Their approach highlighted valuation relevance, which is the information usefulness of disclosures to analysts (much the same as the research objectives of this current study). Valuation relevance allows for a discussion of factors that may not necessarily have a direct relationship with share price but nonetheless may be useful to analysts in their overall valuation process. On the other hand, value relevance rests on statistical relationships between information and market value. Murray et al. (2006) find that there is no direct relationship between share returns and disclosure, although longitudinal data do show a relationship between consistently high (low) returns and the predilection to high (low) disclosure.

Earlier studies on the value relevance of voluntary disclosure find mixed evidence for the value relevance of voluntary, non-financial information. Gray, S. J. et al. (1995) find that non-financial information is directed more towards a company's social accountability, which can, in turn, have a bottom line significance and affect share value. Richardson et al. (1999: 21) develop a model of CSR to capital market responses, asserting that, 'the release of information about any value relevant aspect of the firm, including CSR, has a direct impact on the way in which markets for equity operate'. Rippington and Taffler (1995) examine the usefulness of the annual report and its impact on share price. They find that while there is little impact on share price of the annual report release per se, impact is highlighted from new information coming from the annual report, such as the chairman's report. For further discussion of value relevance see also Orlitsky and Benjamin (2001), Lorraine et al. (2004), and Toms (2002).

Reflecting on analysts' use of disclosures, Holland (1998) finds that private disclosure to financial intermediaries is a significant part of the information process (see also Solomon and Solomon 2006). On the limitations of annual reports, Holland says that, 'the financial report has become too complex, too large and too cumbersome for many users and a source of overload' (Holland 1998: 262). Despite this, the annual report is recognised as a central component in the disclosure system as a 'first layer of understanding' (Holland 1998: 264).

2.2 ANNUAL REPORTS' CONTENT AND READERSHIP

There is a substantial literature on voluntary reporting in annual reports and a small but still significant body of research exists on the actual role of the annual report. In a research report such as this, it is stressed that it is not possible to present a full and exhaustive discussion of this literature but rather to introduce some of the key questions and findings from previous work by way of introduction to the main presentation of evidence from the analysts interviewed for this research.

An early call for research in this area is made by Day (1986: 295) when she concluded that, 'little [up to 1986] has been written about what users themselves appear to find useful [in an annual report]'. Work reporting on empirical studies, typically employing content analysis-based instruments for the recording of content, are usually unable to interrogate user perspectives, although these studies do provide the evidence that most categories of voluntary narrative were increasing over time. It was probably assumed that the intensification of scrutiny of the corporate sector generally was a major cause of increased reporting (Campbell 2004; Tilt 1994) but there was, until some time after Day's call, little evidence of user perspectives on the increased disclosure.

While a small number of studies analyse non-economic stakeholders' perceptions of reporting (eg Tilt 1994), the body of literature referred to in this report is concerned primarily with the reactions of stakeholders with an economic interest in the company. In particular, it refers to stock market participants' reactions to different categories of disclosure. The most frequent inquiry reported upon is that of investment materiality.

Something is known about the general consumption of information in corporate annual reports following work by Bartlett and Chandler (1997), Lee and Tweedie (1975), and Rowbottom and Lymer (2007). Both Bartlett and Chandler (1997) and Lee and Tweedie (1975) examine the behaviour of private investors rather than professional analysts. Both studies find little evidence that the annual report is systematically read, but the Bartlett and Chandler study (1997) finds that more voluntary disclosure is neither needed nor used. They single out the corporate governance section for specific comment, saying (p. 254), 'the sections relating to corporate governance seem to have had little impact on shareholders, with 31.9% reading the directors' statement of responsibility (but only 5.8% thoroughly), and even fewer (23.5%) reading the corporate governance section (though 8.8% read it thoroughly)'.

Rowbottom and Lymer (2007) use a website usage interrogation method to measure the download frequency of the major items in corporate annual reports, a method made possible by the fact that annual reports are broken down into downloadable 'chunks' on the websites. Based on a sample of 15 UK companies, Rowbottom and Lymer find that the most frequently downloaded items by all users (not distinguishing between types of annual report reader) are the compulsory financials. The least downloaded items include the chairman's statement, the environmental report and the chief executive's review. The data are shown in Table 2.1. The Rowbottom and Lymer (2007) study uses a cross-sectional sample of 15 companies, and their results provide an interesting illustration of the relative importance of the different types of annual report disclosure.

The research carried out with the bank analysts, fully reported on in Chapter 5 of this report, confirms the lack of attention given to some of the lower ordered items such as the audit report, chairman's statement and governance report. The contents of Table 2.1 and more specifically their order, should not be regarded as a 'shopping list' effect with the reader stopping when they have enough comfort in the 'basket'. Rather, it signals the materiality placed by users on individual sections of the annual report and its use. Moreover, the relative apparent immateriality of these items is subsequently confirmed in the research findings when the issue of having no 'front end' reporting is discussed with the analysts. There is little evidence that analysts find the 'front end' content to be material but, perhaps more surprisingly, there is little evidence that the voluntary contents are a source of 'comfort' to them either.

Table 2.1: Annual report Web pages requested by users, in order of download frequency (2003 and 2004)

Rank	Item in annual report (in order of downloads)	Type of disclosure
1	Income statement (P&L)	Compulsory, financial
2	Notes to the accounts	Compulsory, financial
3	Balance sheet	Compulsory, financial
4	Segmental analysis	Voluntary,[1] financial
5	Shareholder information	Voluntary, financial
6	Financial year highlights	Voluntary, financial
7	Company profile	Voluntary, narrative
8	Operating and financial review	Voluntary, narrative, financial
9	Five year summary	Voluntary, financial
10	Directors' report	Voluntary,[2] narrative, financial
11	Corporate governance report	Compulsory,[3] narrative, financial
12	Directors' biographies	Voluntary, narrative
13	Remuneration report	Compulsory,[4] financial
14	Chairman's statement	Voluntary, narrative
15	Chief executive's review	Voluntary, narrative
16	Cash flow statement	Compulsory, financial
17	Auditor's report	Compulsory, narrative
18	Statement of total recognised gains and losses	Compulsory, financial
19	Environmental impacts	Voluntary, narrative
20	Financial calendar	Voluntary, chronographic

(Source: Rowbottom and Lymer 2007).

1. Segmental information is now a mandatory disclosure under IFRS 8.
2. The Directors' report is mandatory but much of the content is voluntary.
3. Mandatory under listing rules under 'comply or explain' requirements.
4. Mandatory under listing rules under 'comply or explain' requirements.

3. Calls for research

3.1 CALLS FOR RESEARCH IN THIS AREA

In general terms, previous researchers have identified and stressed the significance of the lacuna addressed by this research. In an early study examining the materiality of social disclosures, Milne and Chan (1999: 440) suggest that, 'little is known about the investment decision impact of narrative social disclosure that firms typically provide in their annual reports'.

More recent research has attempted to address the issue of voluntary narrative materiality but issues with direct access to information users have limited the reliability of findings. Ho and Wong (2004: 62) note that, 'few empirical studies [have examined]… the information needs of users and whether current disclosures satisfy users' needs', while Robb et al. (2001: 80) suggest that, 'further research about the usefulness of nonfinancial disclosures appears warranted'. Such calls were made in response to the limitations of previous research in interrogating the manner in which annual report narrative disclosures were actually consumed by users. Despite the studies described in the foregoing literature review, scholars in the area have been able to highlight the importance of the gap that this present study has attempted to address.

Parker (2005: 856) writes that, 'in terms of the future shaping of the research field itself, there would appear to be ample room for further applications of direct researcher engagement in the field, via qualitative research'. Similarly, Lorraine et al. (2004: 23) remark that, 'qualitative research which investigates companies', investors' and regulators' perspectives on these issues (environmental issues and value relevance) would be worthwhile'. In particular, however, this present research attempts to interrogate views on a range of voluntary narratives, partly in response to Beattie et al.'s suggestion (2004: 233) that 'it would be interesting to elicit from key user groups their views regarding… appropriate weightings to be assigned to each [voluntary non-financial disclosure]'. Accordingly, the importance placed by analysts on a range of categories of voluntary narratives is a key element in the research.

The remainder of this chapter examines the literature on the selected specific categories of voluntary disclosure probed in this research. It begins with that generally regarded as management commentary in nature and then proceeds to examine social and environmental disclosure.

3.2. MATERIALITY OF MANAGEMENT COMMENTARY, DISCUSSION AND STRATEGY REPORTING

A number of disclosure narratives in annual reports are ostensibly intended to provide information on management commentary, performance, strategy, and related issues within these general remits. In all cases, excepting corporate governance and a number of provisions concerning disclosure in the directors' report, the content of these narratives is entirely within the editorial control of management. Unlike social and environmental narratives, which may contain information on non-financial or non-business related activities, management commentaries are all primarily concerned with business-related discussion.

Gray S. J. et al. (1995) suggest that voluntary disclosures can be considered to fall into three categories: strategic information, non-financial information and financial information. While 'capital market pressures do seem to bear on financial reporting practices' (Gray S. J. et al. 1995: 46) in respect of the belief that the cost of capital is thought to be related to disclosure (Botosan 1997), a lacuna appears to exist in the understanding of the manner in which voluntary management commentary is consumed and processed.

In the context of the annual report, disclosures in what Gray S. J. et al. (1995) refer to as strategic and non-financial, include the chairman's statement (the content of which is voluntary), operating and executive review contents, risk reporting and governance issues. The potential importance of these items to investors is significant, although existing research has highlighted a lack of understanding of how the investment community uses the information. Flostrand and Strom (2006) note that, 'the needs of users of business reports were no longer thought to be satisfied with…balance sheets and income statements… [but that] reports now had to include information relevant in predicting the future performance of the firm, whatever form or shape that information might have' (Flostrand and Strom 2006: 582). They continue, 'whilst there are studies testing levels of disclosure it is not known whether this information is useful to one of the primary users of financial information, namely sell-side financial analysts' (see also Vanstraelen et al. 2003).

Risk reporting, for example, is a relatively unexplored category of voluntary disclosure, partly because, as a separate section of the annual report, it is a relatively recent arrival. Whereas in earlier times, management might have mentioned risks in an unspecific, unsystematic or occasional manner, the idea underpinning a risk section of an annual report is partly that all the narrative on risk can be brought together in one place. The valuation of liabilities, provisions and contingencies remain, of course, an important part of the notes to the accounts but the description of risk takes place in the risk reporting section.

A typical risk section lists the risks that the company faces in relatively general terms and then may go on to explain, again in general terms, the way in which the risk will be managed by the company. This may include a note on the internal controls instituted to mitigate internally the effects of the risk. Despite the development of these separate sections, however, academic research has been generally critical of the information content of risk narrative. In particular, that it is too general and contains insufficient information in terms of a quantitative assessment of either the probability of the risk or the impact of the hazard (ie what would happen if the risk event was realised).

Linsley and Shrives (2005) examine risk disclosure in UK annual reports and find that companies did not provide a complete picture of their risks in that 'there is minimal disclosure of quantified risk information' (Linsley and Shrives 2005: 292). Similarly, Woods (2004) finds that, 'narrative [risk] disclosures are generic in nature… and current UK reporting practices are of limited help to users'

(Woods 2004: 373). Linsley et al. (2006) find that, 'general statements of risk management policy dominate the risk disclosures (which are not as useful as specific risk or risk management information)' (Linsley et al. 2006: 280), and they conclude that, 'overall the dominance of statements of general risk management policy and a lack of coherence in the risk narratives implies that a risk information gap exists and consequently stakeholders are unable to adequately assess the risk profile of a company' (p. 387). Schrand and Elliot (1998) point to the voluntary nature and the lack of accounting standards in risk reporting and conclude that companies have no incentive for voluntary disclosures of risk and that risk disclosure, accordingly, is incomplete.

The chairman's statement, similarly, has received a limited amount of attention in the literature. Aerts (1994) identifies the chairman's statement as an opportunity that companies sometimes take to make 'systematically biased' (Aerts 1994: 341) statements and to issue narrative that can be 'coloured' to manage news disclosure in the company's favour. In a later paper (2005), Aerts uses the term, 'self-serving attributional bias' to describe the impression-management efforts that companies, and chairmen in particular, use to manipulate audiences in respect of a particular interpretation of events. Courtis (1998) exercises similar language, referring to the chairman's statement narrative when introducing the 'obfuscation hypothesis'.

There does not appear to be any agreement among scholars as to actual materiality of the chairman's statement, and one reason for this is the intrinsic bias assumed to be a feature. Bettman and Weitz (1983) and D'Aveni and MacMillan (1990) produce contradictory findings when examining the text of chairmen's statements in companies that later went on to become bankrupt, indicating that the text and language style are not related to success or failure. Clatworthy and Jones (2001) challenge Courtis's obfuscation hypothesis when investigating the readability of chairman's statements in the UK. They cannot confirm the finding that disclosures of bad news were more difficult to read than good news. Smith and Taffler (1995), conversely, suggest that the narrative is a potential indicator of performance, although the messages conveyed by the chairman tend to embellish reality. They imply deliberate obfuscation attempts in communicating bad news. In another study, Abrahamson and Amir (1996) conclude that the chairman's statement is a source of 'useful information about the future of the company' (Abrahamson and Amir 1996: 1179).

The evidence for the usefulness of the chairman's statement is therefore mixed. While it can, in principle, be used to convey important strategic information to readers, academic studies that have content analysed chairmen's statements have found that they can be used for conveying biased content or messages that are ambiguous in terms of the future prospects of the business. The apparent scepticism in which the chairman's statement is viewed may be one of the causes of its seeming relative decline in importance in recent decades. Examining the relative importance of information sources used by analysts, the chairman's statement is ranked sixth most important item in an annual report by Lee and Tweedie (1981) and fourth by Arnold and Moizer (1984). Day (1986) finds that the chairman's statement is ranked twenty-first as an item in the annual report referred to by analysts. Although (admittedly) not a direct comparison, Rowbottom and Lymer's study covering 2003/04 (Rowbottom and Lymer 2007) ranks the chairman's statement fourteenth, perhaps confirming a relegation of perception of this item in the minds of annual report readers.

3.3. MATERIALITY OF SOCIAL AND ENVIRONMENTAL REPORTING (GENERALLY)

As one of the most researched areas of voluntary reporting, social and environmental reporting has been studied from a range of angles and perspectives.

There is mixed evidence from the literature on the investment materiality of social and environmental (SE) disclosure. In an early call for research in this area, Dierkes and Antal (1985: 30) argue that, 'the ultimate test for the usefulness of social and environmental reporting information is its impact on decision making' and quite rightly note that at the time of their study there was 'a dearth of information on which to base an assessment of usefulness of this [social and environmental accounting].' Those studies finding generally in favour of SE disclosure being of material interest to investors include Miles et al. (2002) and Solomon and Solomon (2006). Further, Murray et al. (2006: 229) find that, 'although social and environmental disclosure may not yet be an obviously substantive part of mainstream corporate activity, it is a growing concern to all parties.'

Solomon and Solomon (2006) examine the extent to which social, ethical and environmental (SEE) disclosure is integrated into institutional investment. Specifically, the study seeks to evaluate the, 'decision-usefulness of public SEE disclosure'. Based on interviews with 21 buy-side institutional investors, their findings include the observation that, 'there is not enough SEE information provided in company annual reports… [and there is] strong evidence that SEE information was decision-useful and would continue to grow in importance' (Solomon and Solomon 2006: 573). Miles et al. (2002) find a growing demand for SEE disclosure from the investment community and suggest that, 'demand for SEE information has been growing over time'. Further, Miles et al. (2002) argue that SEE disclosure is being increasingly used by institutional investors, underpinning a need to improve the quality and quantity of such disclosure in annual reports.

The stronger evidence from previous research is that which has found largely that SE disclosure is not investment-material in nature. The assumption made appears to be largely that SE disclosure is marginal, 'tagged on', or so perfunctory in content that the information it contains is scarcely of relevance to an investor audience (such as analysts). Murray et al.'s conclusions (2006: 246) include the reflection that, 'if further evidence could be gathered to suggest that markets can be persuaded to start to see the social and environmental implications of their financial decisions then… social and environmental disclosure [would] become a regular, significant and regulated part of corporate disclosure.'

Ho and Wong (2004) report on annual reports usage by Hong Kong-based investment analysts and find very little interest in non-financial voluntary disclosures, including social and environmental narratives. Beattie and Pratt (2002) report the views of analysts, shareholders, financial directors and audit partners of a range of disclosure items. Financial objectives and strategy are found to be the most useful 'with environmental, social and community trailing a long way behind... [and] not seen to be relevant to the investment decision' (Beattie and Pratt 2002: 1)

Milne and Chan (1999) examine the usefulness of social disclosures from annual reports for investment decision-making and find that in some situations, the provision of social disclosure may be associated with fund allocation decisions away from the company disclosing social information. In a paper-based test (ie not involving face-to-face interviews), analysts allocated 'on average 7% of their funds away from the firm that provides corporate social disclosure' (Milne and Chan (1999: 450). They conclude that, 'overall, the results from this study suggest corporate narrative social disclosures do not make much difference to investors' decision making' (p. 451) and, 'only when corporate social disclosure [has] a significant impact on future cashflow will it be perceived as useful' (p. 452)

In a similar study analysing the news direction (good or bad news) of social and environmental disclosures, Chan and Milne (1999) note that: 'UK City analysts... are driven by the requirements of their clients, which they interpret to be primarily a positive financial outcome on the clients' investments. Issues considered moral or emotional are not seen as part of the analyst's remit' (Chan and Milne 1999: 266). Deegan and Rankin (1997) find that social, and especially environmental, information is important to some non-institutional investors but, notably, is of little importance to investment analysts.

3.4. MATERIALITY OF ENVIRONMENTAL REPORTING (SPECIFICALLY)

Whereas many previous studies do not disaggregate the narrative-containing content referring to a range of social and environmental, community, health, safety and ethical issues, a number do seek specifically to examine the effects of environmental narratives on users of annual reports. There are mixed findings on the actual or potential investment materiality of environmental disclosures.

n an industry-specific study, Blacconiere and Patten (1994) analyse whether share prices are systematically affected by environmental disasters. They find that, from a sample of 47 firms, companies with extensive environmental disclosure prior to the Bhopal incident in 1984 experienced a less negative market reaction to the disaster than their counterparts in the chemicals industry who communicated very little about environmental matters. It is this use of environmental disclosure as a part of an organisation's risk management profile that is most often considered to be the most 'useful' use of environmental disclosure as far as analysts are concerned. Studies that have found a link between environmental issues and value relevance include Hughes (2000) and Lorraine et al. (2004), although the value of environmental disclosures was not always supported in terms of value relevance. But, even then, the evidence is scant that environmental disclosures are material in normal market conditions (ie without the perturbations caused by a Bhopal or an Exxon Valdez).

Deegan and Rankin (1997) find that social and especially environmental information is important to non-institutional investors but of little importance to investment analysts. Deegan and Rankin (1999) report that, 'BiE [Business in the Environment] provided evidence that London based financial analysts considered the environmental performance of corporations to be largely irrelevant in determining the investments to recommend to their clients' (Deegan and Rankin (1999: 326). They continue, 'while 73.3% of shareholders and 75% of accounting academics seek this information, stockbrokers and analysts were significantly less likely to seek environmental information within the annual report than any other group of users' (p. 329).

A study highly relevant to the research described in this report is Thompson and Cowton (2004). They examine the interface between bank lending and demand for environmental information while arguing that there is a strong case for banks to have a particularly acute exposure to environmental issues. The reason for this enhanced exposure, is, they argue, because of the potential risks a bank could become exposed to as a result of its lending. This argument represents a fundamental challenge to the assumptions made in some studies that banking can be considered a 'clean' rather than a 'dirty' industry because its direct activities have relatively little environmental impact.

Thompson and Cowton (2004) identify three types of environmental risk that might have an impact upon a bank. Direct environmental risk is that arising from liability for the remediation of environmental damage to property it has obtained, perhaps by a loan default or similar. Indirect exposure, which Thompson and Cowton suggest is the most common, arises when a company holding loan capital from the lending bank goes out of business as a result of its own environmental risk, perhaps arising from a lawsuit or the costs of implementing a new environmental standard or similar. The difference, as far as the bank is concerned, between direct and indirect exposure is one of the limits of liability. For direct risk, the potential liability may be greater than the initial loan amount – for indirect risk, the liability is limited to the amount already lent. A third category of risk linked to the environment is more difficult to measure but perhaps the most important – that of derived reputational risk (Buxton 1997).

In summary, this research attempts to address a number of the calls for additional research in this area by engaging with a primary annual report user group. The research provides insights into the relative importance of voluntary disclosures that have been widely used in the underpinning literature, covering, among other things, risk, social and environmental issues, strategy and governance.

4. Research questions and method

4.1 RESEARCH QUESTIONS

The research questions raised in this studies, in response to the calls from previous studies, concern the materiality and usefulness of narrative disclosures to sell-side analysts, who are a significant user group of accounting information in the investment supply chain. In particular, it was decided that evidence should be sought on the narratives that have constituted the major part of the academic interest in narrative reporting, which are:

- the chairman's statement and strategy reporting
- risk reporting
- social and environmental disclosure
- corporate governance content
- the importance of narrative reporting generally.

It was helpful, when guiding each discussion with the analysts, to divide the conversation into sections, which meant introducing each 'category' of voluntary disclosure and asking specifically about that. To this end, social and environmental disclosures and governance disclosures were discussed separately with the analysts rather than combining them. This approach is consistent with previous and current literature reflecting two distinct areas of study. While there may be overlaps between the two categories, this could be the same for any of the voluntary disclosure areas, for instance risk and governance. In keeping with the objectives of the research, it was necessary to identify and discuss individual categories of voluntary disclosure and to gather evidence on their usefulness or otherwise to analysts as information users. To combine categories would serve to lose this detail and resolution of opinion.

The chairman's statement is voluntary although universally adopted and there is no mandatory content prescription. Corporate governance disclosure, which has grown in volume substantially in recent years, is required in the UK under the provisions of the relevant corporate governance codes (notably by the contents of the FRC's *Combined Code 2003*) under 'comply or explain'. Risk reporting, social, community and environmental reporting are entirely voluntary, although some companies wishing to comply with voluntary reporting frameworks such as the Global Reporting Initiative (GRI) may include some content to ensure compliance.

A more problematic issue to resolve was the sectoral representation of the analysts in the sample. While a broad sectoral sample would superficially appear to be a desirable quality of the sample, it was preferred instead to concentrate on just one, albeit major, sector for the study. This was for two main reasons.

First, a single sectoral representation would enable intra-industry observations to be made, the reliability of which would increase with repetition by sample members. Second, it would enable the information needs of one particular cohort of sectoral analysts to be examined in detail, which would not be possible were analysts to be drawn from across a range of sectors. Additionally, with the numbers of London-based sell-side analysts representing the major investment houses in any given sector being relatively low, it was a happy possibility that the sample chosen for interview would approximate to the population, thus providing the maximum possible reliability of findings for that sector, given the number of participating bank analysts in the research. In total 19 sell-side banking analysts were interviewed. As at July 2008, Alliance and Leicester plc listed individual analysts in 18 firms that provided analyst coverage and Barclays plc provided a similar list of 23 firms. All the analysts interviewed for this research were from firms named as providing coverage.

The four major 'volume' areas of analysis in London are technology, pharmaceuticals, oil/gas and banks. For this study, it was decided to focus attention on the analysts of UK banks. This was for two reasons. First, it would facilitate the interrogation of the perspectives and views of a high proportion of the London-based analysts of a strategically important sector for the UK and European economy (see Centre for Economics and Business Research 2007). In terms of market values as at the end of 2007, banks represented approximately 15% of the total FTSE 100 value.[1] Second, there are ample reasons why all the narrative disclosures under consideration in this research could be material and/or useful to investors. The chairman's statement may contain important strategy disclosure; risk reporting may contain risks previously unknown to analysts that are capable of affecting returns, while social and environmental reporting may affect the bank's risk exposure (depending on the environmental risks associated with loans) and the reputation of the bank as a responsible social and environmental 'citizen'. Corporate governance is potentially the most perfunctory of the reporting categories taking into account that compliance with the *Combined Code* can be considered a 'box-ticking' exercise.

4.2 METHOD

It was necessary to gain access to a number of analysts so as to establish their views on the subjects of the research questions. In order to identify a cohort of analysts to approach, the list of analysts that covered Alliance & Leicester plc was used as a starting point (the list was, happily, available on the Alliance & Leicester website). On contacting the analysts on the list by telephone, it became clear that most also covered other UK high street retail banks and it emerged that the list was a fair approximation to the population of UK bank analysts in the City of London.

1. Based on banks' collective valuation of £212 billion against a FTSE 100 value of £1,472 billion.

On having the nature of the project briefly explained to them over the phone, all but one of the analysts on the list agreed to be interviewed. The interviews took place at the London office of each analyst between the autumn of 2004 and the summer of 2006. Once a small number of analysts had been removed from consideration for reasons of non-availability (such as retirement, career moves, etc.), the number of possible suitable analysts was 20. Allowing for the one refusal, the final number of analysts interviewed for the project was 19. Each analyst was interviewed by one or both of the two researchers conducting the study.

At the start of each interview, the analyst was initially assured that his or her evidence would be fully anonymised and accordingly, they could speak freely on their views about the matters in question. After that, a recent annual report of a bank covered by the analyst was produced by the interviewer and the analyst was invited to describe how they would use the document if that was the first time they had seen it.

The Alliance & Leicester plc annual report and accounts for year end 2003 was used for this purpose. This was for two reasons. First, it contained examples of all of the categories of narrative disclosure being studied and second, it was manageable in size in comparison with some of the other, substantially more voluminous tomes that are produced by some banks (notably by HSBC).

The analysts spoke uninterrupted for as long as they wanted in response to the first request. Following that, a number of follow-up questions were asked to establish each analyst's views on the usefulness, and more specifically on the materiality, of each disclosure category and of narrative reporting in general to them as analysts. In this respect, each encounter was similar to a semi-structured interview in terms of research method. A standard list of questions was asked, clarifications were sought and occasional tangential diversions were indulged in. Each encounter was good-natured and cordial containing both informal and semi-formal exchanges. All interviews were recorded in their entirety and subsequently transcribed. A typical encounter lasted a total of one hour.

5. Evidence from analysts

5.1 THE COHORT AND GENERAL PERCEPTIONS OF THE ANNUAL REPORT

The cohort of analysts interviewed for this research had an average of 8.5 years' experience in the job. The majority were not professionally qualified in accounting although all were qualified to degree level or higher. The most common academic backgrounds of interviewees were (in order) economics, maths, finance, accounting and law.

Almost all the analysts interviewed discussed the limitations of the annual report in terms of the timing of its publication. While the year-end results are accompanied by the preliminary accounts ('prelims', which include narrative contents), the final printed version of the annual report and accounts is often not published until some weeks later, by which time the information in the prelims has formed the basis of the analysts' forecasts. This publication lag significantly reduces the usefulness of the final document as an investment-material source of information. The detail in the preliminaries and the information conveyed by management at the results presentation are far more important in the intervening period.

Analyst A2 noted:

> *On the basis that you get your report and accounts after you've already had the preliminary results, you are two months down the line from when you were actually given the specific… information in the preliminary results*

Analyst A5 stated bluntly:

> *Well I wouldn't use that document* [the annual report] *to start with because… the results typically come out in February and this is published in April. So is it a major event? No.*

Analyst A16:

> *From my point of view the annual report rarely gets used in the way I've just described … to you* [which was a detailed illustration of how each section could be technically used]. *To me it's more a way of getting hard detail and you know by the time it's out it's been fully audited and there's no way that they're going to revise anything.*

Most, however, took a less strident view than this, with the majority referring to the document variously as potentially important for new information that is most likely to be in the detail and possibly in the notes to the accounts. In this regard, it is used as a historical document that contains more detail than the preliminaries.

Analyst A5 went on to say:

> *Now where the annual report comes in far more useful is where, for instance, you say, have Barclays or Royal Bank of Scotland. The companies… don't publish their annual report on the actual day. You therefore go back to it … to look through things in a lot more detail in terms of that kind of information.*

Despite the limitations caused by the publication lag, the contents of the annual report in general were considered by most to be potentially highly material to the investment decision, although the cohort differed substantially in the use they made of the document.

Analyst A12's remark was typical:

> *I would say it's highly material. As an analyst there are two opportunities each year to really understand how a company's doing. One is the interim results; one is the final results. And most of our forecast revision, most of our recommendation changes I think are driven by what management say at either or both of the results presentations. I would place a high reliance on the annual report. The model which drives our recommendations is basically the annual report but extrapolated, so it's crucial to the model. So I place a high reliance on it and would say it's a very important document indeed.*

Analyst A14's criticism was less to do with the publication timing and rather more to do with their increased length and complexity. Commenting especially on HSBC's weighty annual report, Analyst A14 remarked:

> *To be honest the annual report bit would probably score pretty lowly* [in terms of usefulness to me]*: a 1 or a 2* [out of 10]. *I've given up on how many times I've got* [this sort of] *message back from HSBC in response to my question: 'If you go to the US disclosure no. 4, page 232 then you'll find the answer to your question'. Great, fine, but actually I'm still going to continue to email you even if all you do is give me the reference of where it is, because I'm not going to read… there's just way too much to read.*

Analyst A16 also commented on the increased length not necessarily being helpful.

> *This is where banks sometimes get a bit confused because you ask for better disclosure and they think 'oh, look, we've given you 600 pages already'* [which contains] *575 pages of completely worthless guff. What we really want is granularity and in the areas that matter.*

5.2 USE OF FINANCIAL INFORMATION

One of the prominent emphases made by all the analysts in the sample was the overwhelming importance placed upon the numerical financial data in annual reports. This was not a surprising finding insofar as one of the main roles of an analyst is to forecast the key financial statistics over the forthcoming period, and the recent history of those statistics is therefore of utmost interest.

The initial part of each meeting with the analysts was spent asking each interviewee to talk through, in their own words and in their own time, how they would begin to consume the information in the annual report if that had been the first time they had seen that document. This enabled each analyst to highlight what was, to him or her, the section of most material immediate interest. It came as no surprise that each analyst went straight to the financials.

The order varied among the cohort, but in almost all cases, the first 'port of call' was either the income statement or the notes to the accounts. The balance sheet was considered less important in most situations than the income statement and the cash flow statement was generally viewed as less material again. Analyst A1 reported that, 'To be honest as bank analysts we don't tend to look at the cash flow statement too much.' Segmental disclosure was, however, highly valued.

The relative importance of the income statement for earnings and costs forecasts was emphasised by most of the cohort. Analyst A16 was relatively dismissive of the balance sheet in comparison.

> *I don't spend a lot of time digging through the balance sheet. I certainly don't try and forecast the balance sheet on a line-by-line basis* [as I do with the income statement].

Analyst A14 was typical in describing the general approach taken.

> *My normal first port of call is to go into the notes to the accounts because this is the additional disclosure to the prelims... and in particular I'm interested in the balance sheet at the consolidated level and the cash flow at the consolidated level and therefore I would go through the notes to the accounts.*

Similarly, Analyst A7 remarked as follows.

> *P & L accounts, the balance sheet, the notes and in particular the financial review which obviously gives some sort of qualitative discussion around the numbers to at least give some sort of context and explanations in terms of why particular numbers in the accounts and the income statement, etc. have moved in the way in which they do.*

A15 explained the purpose of the financial analysis as trying to get 'a feel for the underlying situation of the company and even then you'll find that some of the numbers we probably will disregard. We will have our own way of calculating [financial statistics]'.

There was a general scepticism about reported figures among most of the cohort. Financial ratios given by the reporting company were never taken at 'face value' and other figures were frequently added back to reported costs and earnings to arrive at what the analysts considered a more reliable figure. Analyst A16, for example, referred to having to 'dig deeper to strip out any of the one-off effects or to get a feel for what the trends are'.

5.3 VIEWS ON THE 'FRONT END' AND GENERAL NARRATIVE REPORTING IN THE ANNUAL REPORT

It was when discussing the annual report content other than the financials that differences of opinion between analysts began to become evident. This is the section of the annual report that has seen the most growth over recent years, as companies have included more and more information on various aspects of their business apart from the purely financial. In this context, 'front end' includes the collective disclosures that take narrative rather than numerical form. Asking each analyst their view on this was intended to gain evidence of their overall views on the importance of narrative reporting in general. In most cases, the 'front end' includes the chairman's statement, possibly a chief executive's review, an operating review, corporate governance disclosure, risk disclosure, health, safety, social and environmental disclosure, and various other narratives that companies include on an ad hoc basis.

This section of the annual report would theoretically be of interest when the information sought is not available in – or cannot be expressed by – the financial information. In practice, much of what is in the narrative sections is content already seen in the preliminaries so it suffers from the same time lag limitation as other content of the annual report as a whole.

Opinions on the materiality and usefulness of 'front end' narrative reporting were mixed in the cohort of analysts.

Analyst A2 spoke for the majority in viewing the contents of the 'front end' as template driven.

> *You almost can get slightly cynical about the questions of box-ticking by executives and what the reasons are for doing that. I would guess that generally, in terms of reporting and information provided, they tend to stick together as a pack* [meaning the categories they disclose are very similar].

Analyst A13 expressed a similar view.

> *But in terms of the sections which are solid text in terms of, say, 'our policy' as regards the environment or our employees or our shareholders – most of that tends to be template-driven stuff.*

Analyst A9 said that the narrative form of the 'front end' was one of the reasons for its not being widely used by analysts.

> *There are things that need to be here and maybe once every three years you might* [read it] *because you have a specific issue and you go here* [to find something out]. *If I get this report would I look at it in great detail? No. But where we come from we are much more about numbers – I want to see the numbers.*

Analyst A15 suggested that there may be an audience issue with the materiality of 'front end' narrative reporting, referring to the information needs of independent shareholders (not dealing through fund managers) and the specific information needs of analysts.

> *If you are looking at it as an independent shareholder you will concentrate, as I say, on the first 30 pages of the blurb. As an analyst, given that we probably know all of that…the first 30 pages will probably never get read.*

Interviewer: 'So front end voluntary? Not interested?'

> *Completely not interested. I could probably say that I have not read any of those.*

Analyst A10 expressed a similar view, saying, 'it is exceptionally rare that I'd actually look at anything in the front pages', while Analyst A14 saw most of the 'front end' as something that might be perused briefly but then kept as a source of information:

> *The director's report largely is a skip-through. As I say it's not something I would go to and read specifically first but its good to have it there as a reference.*

Analyst A4 was critical of the perfunctory and redundant nature of some of the narrative contents.

> *There's a lot of rubbish actually that could have been in there* [the Alliance & Leicester annual report] *but wasn't. HSBC are swines for bulking the whole thing out* [with less than useful content].

Analyst A8 was critical of the narrative content of the reports because of potential issues that could arise owing not only to undisclosed management motives but also to audit requirements.

> *Those* [narrative sections] *are read with a sceptical eye because companies rarely admit when things are going wrong until they've gone so badly wrong that the management who'd got them wrong have been fired and the new guys come in and* [say] *'oh that was a terrible idea'. But yes, of course, a lot of the feel for what's going on in the business is up front, not down the back* [of the report] *but as we discussed, the segmental reports are unaudited so they're at the front not the back generally.*

Analyst A8 went on to describe some of the concerns with narrative reporting generally.

> *I would say companies consistently strive to position themselves in a favourable light, so that you have discretion to describe things as you see them and to put more emphasis on the things that are going well than the things that are going less well. So* [while]*… I would absolutely not… accuse the companies of lying, I would accuse the companies of indulging in self-promotion.*

Despite these misgivings, however, the consensus overall view was that the 'front end' was capable of containing content of material use to analysts. Analyst A17 gave an example of this.

> *But what we look for in there is any statement about the outlook and any statement about management or on targets. That is actually very important.*

The importance of strategy content in the annual report is discussed in the next section.

5.4 CHAIRMAN'S STATEMENT AND STRATEGY DISCLOSURE

The chairman's statement is one of the most-discussed and researched elements of the annual report 'front end' in the literature. It has been analysed in terms of readability, bias and news direction (see in the discussion of the literature above). There is neither prescription in company law nor listing rules about the content of the chairman's statement. In practice, chairmen have typically used the statement (or 'letter') as a vehicle for summarising the previous year's performance, to highlight any key changes, to acknowledge those who have contributed to any successes and to comment on 'going concern' and future prospect issues over the subsequent year.

Analyst A13 summarised the importance of the chairman's statement in the annual report.

> *Well, I think he* [the chairman] *has a moral duty… to communicate with shareholders, to put his name to the annual report and say 'this is mine' and 'I'm upfront and this is how I'm leading the organisation'. The second reason would be that they will have a significant number of shareholders whose only substantive communication with the company will be this* [document, the annual report] *every year: people who own the stock on their own account and who are not sophisticated followers of the market.*

While the majority of the cohort of analysts made comments similar to those of Analyst A13, there was a considerable and prevailing expression of scepticism over the value of the content. The most oft-cited reason for this scepticism was the lack of strategy content and, for this reason, most analysts compared the chairman's statement unfavourably with the usually more detailed chief executive's review.

In the quest for greater detail and granularity, most of the analysts were dismissive of the chairman's statement as less than material, with some reserving some relatively unmeasured language for it.

Analyst A3 began by commenting that the chairman's statement was 'bloody irrelevant' before proceeding to clarify this remark by citing the sections of a typical chairman's statement.

> *Well the chairman's statement tends not to* [contain strategy] *does it? 'Economic outlook', well, thank you I've got a fair idea myself. 'Results' I can read. 'Capital and dividend' I know you're double A-rated or whatever. 'Our people', 'Board changes', 'Realising our potential': yes. I*

> *suppose 'Realising our potential' could have been interesting* [but wasn't].

Analyst A13 provided a helpful summary of the way in which most analysts view the chairman's statement.

> *Well, we certainly read it but I've yet to read one that tells us anything that we either weren't told at an analysts' meeting two months before the financials came out or that isn't part of a communicated strategy that's been around for ages. So you look at the two pages that we have here from the chairman: 'Economic outlook' – we have economists that do that; 'Results of the company' would have been enunciated at their meeting and we would know all about that; 'Capital and dividend' is extraordinarily important for* [a bank] *and so we would have a look at that but again because it's so important. Typically the wording we won't have seen before – that would be the most important component of that. 'Our people are valued'* [and] *'Board changes', again, tend not to be all that material particularly when it's on the non-executive side of things. 'Realising our potential', you know, I hope they do!*

Analyst A13 said that the chairman's statement 'isn't the place where you're going to see a change in policy or a change in strategy.' Analyst A9 said it was 'too woolly; it doesn't tell you much'. Analyst A7 spoke for the majority, referring to its potential materiality as 'limited', while Analyst A15 preferred the term 'useless'. Similarly, Analyst A4 remarked, 'nine times out of ten [the chairman's statement] would be useless' with similar disdain by Analyst A5, who simply said, 'I tend not to focus on this as an analyst'. Analyst A14, perhaps with a little overstatement for effect said, 'I don't think that I've ever read one'. Another direct criticism was made by Analyst A16 who said, 'I find [it] usually not that helpful... I tend not to focus hugely on the chairman's statement.' When, in conclusion, Analyst A12 was asked, 'So is the chairman's statement immaterial for the most part?', the reply was, 'I think so, yes'. Analyst A4 concluded that the chairman's statement was 'worthless as far as I'm concerned'.

The most usual reason for the dismissal of the chairman's statement as a material and useful disclosure was its lack of detail and its cursory treatment of information on the company's strategy. For this reason, some analysts compared it unfavourably with the often more useful (and, in contrast to the chairman's statement, voluntary) chief executive's review. The fact that this particular piece of voluntary narrative has effectively become a fixture of the annual report, typically under an 'operating and financial review' section or similar, was greatly welcomed.

Analyst A12 remarked, 'The chairman's statement I'd sort of regard as a slightly watered down version of the CE's statement,' while Analyst A16 commented, 'what the chief executive says is definitely more interesting and more relevant to me'. Analyst A3's comment was based on the Alliance & Leicester plc 2003 accounts that were used as a basis for the discussion:

> *The strategy bit of the chairman's statement is like those five column inches. You turn over to what* [the CEO] *is saying* [which includes] *'management priorities, managing the portfolio, maintaining building, profitability, position...' I mean you've got a full two pages overleaf from the CEO.*

Analyst A4 highlighted the typical content of the chief executive's report in explaining its usefulness:

> *Chief Executive's review – more interesting* [than the chairman's statement]. [I] *wouldn't necessarily read that first but probably would try and read it, not least because that usually is where you get them admitting to missing targets or saying what targets they've made and that's where you get targets for the future.*

A similar remark was made by Analyst A18: '[The chief executive's statement] usually has a brief summary of what's happened in the year past and any big events that they expect for the next year.'

5.5 RISK DISCLOSURE

Risk disclosure and risk management information are two of the most notable additions to the voluntary content of annual reports since the mid-1990s. Whereas previously, company officers might have made reference, in an unsystematic manner, to risks as part of their overall discussion, the segregation of risk information into a dedicated section is a relatively recent innovation. The banks' reports that were discussed during conversations with the analysts were typical of other annual reports in containing a separate page or more of narrative reporting on this subject.

In almost all cases, risk reporting in the 'front end' of the annual report is entirely narrative in nature, and numbers, where relevant, are confined to the notes to the accounts. In the Alliance & Leicester accounts that were used as the basis for discussion, the risk reporting comprised narrative sections on operational risk, credit risk, market risk, interest rate risk, foreign exchange risk, equity risk, liquidity risk and derivatives. Each section contained a definition of the type of risk in question and this was usually followed by an indication of company policy in respect of the risk and typical actions taken to gather intelligence on it. The discussion of operational risk in the Alliance and Leicester accounts, for example, contained three paragraphs that respectively began: 'Operational risk is defined as...', 'The Group monitors its operational risk through a variety of techniques...' and 'Operational risk is managed through a combination of internal controls...'

While recognising that this narrative tends to be template driven, the analysts expressed a range of opinions on this particular category of narrative reporting. Although, prima facie, risk disclosure might be considered to be naturally material in the banking sector, the majority of analysts expressed scepticism about narrative risk reporting in the annual report. A typical opinion was that risk reporting was simply a boiler-plating or a box-ticking exercise performed annually by companies without any real attempt to report either on the actual changes in risk exposure over the year or as anticipated in the year ahead. Most of the analysts relied on their own sector-relevant knowledge of banking risks and risk management, and viewed disclosure as being, for the most part, meaningless to them. Moreover, the levels of disclosure were often regarded as being too simplistic for analysts on the one hand but perhaps too complex for the individual non-specialist investor on the other. In this respect, it was suggested that risk reporting failed as a material disclosure for both types of annual report user. Analyst A5 pointed to the pro forma-driven content and suggested that, 'if I as an analyst didn't know what the risks were in a bank I wouldn't be employed by the bank I work for.'

Referring to the risk narrative, Analyst A5 continued, 'that's generic what's written there, and it's probably not even a very good description of [risk] to someone who didn't really understand [such as an independent investor]. Does it really tell you anything? No.' One possible reason for the limitations of risk narrative content was suggested by Analyst A18 who said, 'the risk section… should be more interesting but it usually tends not to be because they never give anything away and that is the problem'. Analyst A11 remarked that, 'a lot of it is stating the obvious a lot of the time' and Analyst A12 opined, 'I think it's mostly common sense'.

Frustration with the shallow and perfunctory nature of risk content was raised by several analysts. Analyst A4 made a general criticism:

> *then we are immediately into risk management and control, which is almost always useless. So we've got pages on foreign exchange rates, tax derivatives and uses. Realistically there is nothing that you can say from the outside about how someone else's treasury is working. This stuff is just completely useless.*

Analyst A3:

> *For people who are risk management fetishists, I'm sure it's good to have and in terms of ticking boxes* [and] *it seems to be a useful exercise. This must be infuriating for the banks having to do* [this] *because they'll probably sit there, roll their eyes and scribble down whatever fits the relevant boxes.*

Analyst A7:

> *Risk management and control, which is probably 2, 3, 4 pages worth of how they deal with and manage equity response, exchange risk, interest rate risk.* [My criticisms are]*: a) it doesn't tend to change very much from year to year,* [and] *b), frankly most of this stuff is pretty common from bank to bank. Once you've read it once, you've probably read it as many times as you want to and it does very much tend to have this sense of being boiler-plating.*

Analyst A17:

> *They just copy them from year to year so when they do the accounts they say 'oh we have to put in this' and they take last year's and just put them, in which means we've already read them* [in last year's accounts].

Analyst A3 hinted that one reason for the poverty of disclosure was the complexity of the banking business.

> *If you want a decent discussion of risk management within banks you kind of need to be a banker already to understand it because they are inherently very complicated businesses.*

There was, nevertheless, a general feeling that the presence of risk narrative was a potential source of comfort to analysts even though the content was probably not of direct material interest. Analyst A11 was typical in expressing the view: 'I think it's important to have it in because I think it makes banks think about those risks'. And similarly, Analyst A16 remarked that, 'the fact that it's there – you see it's there, you know it's there – it gives you some comfort that somebody has thought about it'.

When the question of reading the actual risk narrative reporting was raised, however, the general view was that analysts did not read it. Analyst A14 struck a sceptical note, saying, 'I don't think I've ever read much on operational risk but I certainly never remember reading anything useful in there.' Analyst A4 described the content as being of 'little use' and Analyst A16, on being asked whether he or she ever read the risk reporting narrative, commented, 'Probably not to be honest; probably not'.

A potential use of risk reporting was suggested by Analyst A4 in expressing frustration with dealing with investor relations (IR) people in some banks.

> *What I would like to see – and I've seen it absolutely nowhere – is you always have to drag these statements out of the IR people and its always like pulling teeth to get them to say something. Simple things like: do you hedge the following foreign exchange risk* [example of foreign exchange risk given]*?*

Finally, only one analyst (Analyst A1) in the cohort of 19 expressed something approximating to a positive view of the current state of risk reporting.

Interviewer: 'Do you look at risk disclosure?'

> *Yes. The risk section is a key section in terms of country exposure, sector exposure and… trading risk as well. Those are all in there… and the risk management and control* [and] *operating risk* [are items] *that, yes, you'd look through.*

5.6 CORPORATE GOVERNANCE DISCLOSURE

Disclosure on corporate governance issues has been in the ascendant since the early 1990s when these issues first became of concern in the light of the *Cadbury Report* (1992) and since. The manner in which corporate governance content has been presented has become increasingly complex and organised in recent years as companies have sought to comply both with the range of (legally) voluntary codes and increased market expectations. Codes of practice in corporate governance have included those on executive remuneration, non-executive directors, committee structures, internal control and reporting. In each case, the codes provide for the disclosure of information pertaining to that area in the annual report.

In the UK, corporate governance code compliance is voluntary in law but effectively mandatory under stock market listing rules (this being the nature of control in a principles-based jurisdiction). Although technically, companies can 'comply or explain', in practice large companies, and perhaps especially banks, normally comply to a high degree to maximise market confidence. One of the results of the increasing number of corporate governance codes since 1991 has been a substantial volumetric increase in corporate governance reporting. In contrast to some other sections of 'front end' reporting, corporate governance reporting is often numerical in part (reporting on executive salaries, for example) and its content is effectively prescribed by the various contents of the various codes of practice.

One reason why corporate governance in the banking sector has been a matter of historical concern to stock market participants was the collapse of a bank (the Bank of Credit and Commerce International – BCCI) in 1991, which was one of the causes of increased regulation. Analyst A2 drew attention to this, saying:

> *there have been banking disasters,* [such as] *BCCI, but I guess I'm starting* [these days] *with an implicit or assumed confidence* [in banks' corporate governance]. *It might be misplaced but there have been one or two cases.*

Analyst A12, similarly, opined, 'I think corporate governance is an important issue. We've had scandals in the bank sector that proved it is important.' This research was undertaken before concerns about Northern Rock emerged in the autumn of 2007.

The evidence from the cohort of analysts was that the increased corporate governance requirements including and since Cadbury had served to increase confidence in governance systems. Analyst A3's confidence was signified by the comment, 'corporate governance? Don't care that much in the UK'. Analyst A6 said that, 'it [corporate governance] doesn't tend to be an issue in the UK' and Analyst A12 stated bluntly, 'I have confidence in the banks' corporate governance structures'. Analyst A2 spoke for the majority saying, 'I'm not aware of that many cases of major corporate governance problems with a bank'. When Analyst A13 was asked: 'so you have full confidence in the corporate governance in UK banking?' the reply was, 'In so far as it's important, yes'.

Several analysts brought out the confidence of corporate governance in UK-based banks. Because most of the cohort covered only these banks, they were not able to comment on corporate governance in other jurisdictions with lesser governance provisions. Analyst A6 said that:

> *because we cover UK and Irish banks and it's certainly less relevant from our point of view. But yes, I think undeniably it obviously becomes important where corporate governance might be an issue* [such as in some other jurisdictions].

With regard to reporting, the prevailing view was that while the presence of corporate governance content was important, it was of little materiality or use to the cohort of analysts. Analyst A7 said:

> *it's of very limited interest to me to be absolutely honest. There's very little here that I would actually tend to use… the statement of corporate governance is usually fairly low-value.*

Analyst A6 was more laconic: 'Do I use it? No. Do I think it is important for it to be there? Yes'.

Others expressed blunter opinions, saying that they didn't read the corporate governance content at all. Analyst A7 said, 'I don't tend to look at that at all'. Analyst A12 gave more detail, saying:

> *I do not read the corporate governance disclosures. I take the assumption that these companies are FTSE 100 companies, they're going to have pretty much the systems that they need and I'm happy to rely on that assumption.*

Analyst A15 was in a minority, expressing the view that the statement of corporate governance was 'useless'.

5.7 SOCIAL AND ENVIRONMENTAL (SE) DISCLOSURE

While the subject of social, environmental and ethical reporting has increasingly been of interest to academic researchers, there has been relatively infrequent interrogation of user cohorts as to its usefulness and materiality. The evidence offered by the analysts in this study suggests a range of responses to this reporting category, but the prevailing belief is that both social and environmental matters are of limited interest to the professional analyst and forecaster. Probing the reasons for this lack of interest was one of the most intriguing parts of this research project. In organising the evidence in this disclosure category, content is set out in five subsections:

- whether SE narrative is used and its materiality
- evidence that some analysts may misunderstand the nature of SE narrative
- environmental risk and disclosure
- the potential (rather than the current) materiality of SE reporting, and
- the way in which SE reporting is seen in the context of the whole annual report.

Use made, and materiality of, SE narrative reporting
Analyst A2 put the issue in some kind of context, saying:

> *as I say banks, although they do have a part in the social fabric and so on… – the whole kind of stakeholder idea – for what I'm trying to do* [social and environmental reporting is] *not that relevant really.*

Analyst A15, as part of a commentary on his or her use of annual report contents said, 'corporate social responsibility report? Even more useless [than the chairman's statement and corporate governance].' Analyst A17 said, 'it sounds bad but from our point of view at the moment this CSR/ environmental [disclosure] is close to useless.'

Analyst A14 expressed this view: 'Corporate and social responsibility report? Forget it. Just forget it' after which the interviewer pressed, 'Is CSR reporting totally useless to you?' 'Yes!'

Upon probing in a little depth, it became apparent that social and environmental reporting was, for the cohort of analysts, perhaps the least read and least relevant part of the entire annual report. Analyst A1 was asked 'Are you interested in social and environmental disclosure at all?' which received the reply, 'Not really, no.' Analyst A2 said, 'Frankly I'd ignore it really' and Analyst A4 said that 'Corporate and social [disclosure was] definitely no use.' Analyst A7 reported that it was 'absolutely useless from my point of view'.

Analyst A4 continued with a commentary.

> *Business ethics* [quoting from the narrative] *blah blah blah. I'm not being funny but it just would never occur to me to look at that. There might be something incredibly useful in here but I would bet money that there isn't!* [So] *corporate social* [disclosure is] *definitely no use. I've been a analyst now for eight years and it has come up in conversation exactly once during that time.*

Analyst A1 confessed that:

> *I've never really looked at one* [a social and environmental report] *before so I could be just alone* [in my view, but] *we've got so many pressures on our time that it's quite low in our list of priorities to actually read through that and if you've got to read the whole report that's going to be the last* [thing you would read].

Analyst A6 claimed to read the social and environmental report, 'very, very rarely… actually I don't think I've ever read through one'. Analyst A10 said of social and environmental reporting, 'don't give a damn. Personally I might give a damn. Professionally I don't care.' Analyst A11 said, 'very laudable but I'm not interested', Analyst A13's view was that 'speaking purely from an investment analyst perspective it's not useful at all', and Analyst A12 said 'I don't read that part of the account.' Similarly, Analyst A16 said: 'I can't see any value in that section. I've probably never read one'.

Specifically with regard to environmental disclosure, Analyst A4 was as dismissive as he or she had been for the rest of the business ethics reporting (in the annual report being discussed): 'Environmental blah blah blah. It's a bank,' implying that this identity had a bearing on its interest in environmental matters. Analyst A13 said that environmental narrative was 'even less useful' than the social and ethical components. Analyst A14's view was: 'I think… it's a waste of money to be printing a lot of this, and also, I suppose there's a kind of irony in printing an environmental report that nobody reads'.

With specific regard to social and environmental narrative and the question of materiality, the consensus view was that it was perhaps the least material (actual or potential) component of the annual report. There were, according to the cohort, a small number of situations in which it could be material to investment decisions but these were considered to be marginal: analysing for socially responsible funds or when a specific environmental risk applies. Analyst A6 reported that, 'if the client's funds aren't socially responsible… then this sort of stuff is obviously somewhat less relevant to an extent from that [materiality] point of view'.

Analyst A5 was asked: 'So in terms of your work as an analyst how you would judge the CSR component [of the annual report]?'

> *Not material at all. There might be analysts out there who sit and read this from cover to cover but is there anything in here material that's going to affect the share price? No.*

Analyst A9 highlighted a limitation of all narrative reporting, to analysts, with specific reference to social and environmental content, saying that, 'These are more soft issues and they wouldn't be driving the [forecasting] model. We are about numbers. We are putting numbers in a spreadsheet and coming up with a forecast.' The implication of this comment is that unlike some other narratives, social and environmental reporting is unlikely to contain information capable of amending or informing any aspect of the financial forecasting model. In this respect, it seems there is a weak belief that any important environmental risks would be discussed in the social and environmental narrative.

Analyst A12 expanded on this belief.

> *I know that there is an increasing demand in the market for ethical investment and those sorts of disclosures can help convince people of the ethics of investing in companies but we're really interested in financial performance and valuation. I'm not convinced that at the moment those sorts of considerations* [such as] *CSR disclosures drive share prices.*

Analyst A18 expressed a similar view.

> *I wouldn't say they were completely useless but nothing from those sections go*[es] *into our models on how the companies work. We never write about that section at all.*

Misunderstanding of SE reporting

A small amount of evidence emerged that analysts, in their unwillingness (in some cases) to read the social and environmental section of an annual report, may have misunderstood its content. Whereas in fact many reporting organisations, including banks, report on the environmental impact of their activities, some analysts appeared to judge social and environmental reporting on its most perfunctory content.

Analyst A4, for example, was dismissive, saying:

> *Looking at it, it's just sort of 'for customers who are deaf, hard of hearing or have speech impediments, a fully qualified sign language interpreter is available on request'.*

Analyst A14 was seemingly unaware of the more detailed content of social and environmental reporting that has been introduced in recent years.

> *I don't think that corporate social responsibility has any bearing on socially responsible investor issues because its all about how much paper – well I'm guessing because I haven't read one – but I'm guessing its all about how much paper they've used and all this kind of stuff. Terribly irrelevant.*

Environmental disclosure and secondary environmental risk

One of the particular issues that the researchers wanted to explore with the cohort was the importance placed on a bank's environmental exposure through its loan book rather than through its direct operations. For the purposes of clarity, direct environmental impact is defined as that applying to the actual operation of the organisation's main direct operations. For a bank, this would be the environmental impact of its own employees in the normal pursuit of activities.

The point raised by Thompson and Cowton (2004), however, was that, uniquely, banks had a potentially large secondary or indirect environmental footprint in the activities that are facilitated or enabled through loans made. Analyst A3 was asked about the general environmental risks for a bank. The answer was typical of those failing to recognise indirect environmental risk.

Interviewer: You wouldn't see environmental risk as part of the risk of the business at all?

> *Not really in a bank. Certainly if it was like a nuclear power station or an oil company I might worry about it a bit more.*

Analyst A9 gave a blunt answer to the question of whether he or she would ever consider that banks might be complicit in pollution or expose themselves to environmental risks by their lending decisions, saying, 'No. Straightforward answer. No.'

Analyst A3 explained that:

> *I think these guys are bankers not some sort of environmental guardians. That is probably something that's far better controlled by other parties. I think it would be harsh of banks to try and work it* [secondary environmental impact] *out because when I think about investing in a bank I'm thinking about how it's going to create money using my money.*

Analyst A17 expressed similar misgivings, saying:

> *If banks by their lending can be held accountable for what the company does with the loan that would make it close to impossible for banks to do anything. The environmental impact, just doing the actual report they would have to use half an entire rain forest just to publish the report.*

Analyst A18's view was that it was not a bank's purpose to moderate lending activity using environmental criteria.

> *I think to be honest that is the government's job to regulate what industry does and I think ultimately the management of any company should try and maximise shareholder value.*

Analyst A13 was asked whether he or she could ever envisage a situation where the environmental exposure from the loan book would ever be material to an analyst's forecasts: 'From my perspective, and certainly given the tasks I have, I can't imagine it ever being material.'

Potential materiality of SE disclosure

Given the responses from the cohort on the current relevance and materiality of social and environmental narratives, follow-up questions were asked on the situations that may increase their materiality in the future. The only situation at present where SE disclosure would be an annual report item worth analysing would be if it were for a socially or ethically filtered investment fund.

The size of the change needed was highlighted by Analyst A3, who was asked: 'Could you ever see a situation where an environmental disclosure or a community disclosure would ever be material disclosure for you as an analyst?'

Yes I could. It would purely be if it was driven by my clients – if we end up with a huge socially responsible investment community that dominates the landscape. At the moment the sort of people, like you and I, [who] *invest in our pensions* [want] *to have a safe retirement, it may be nice to think about the environment a bit on the side, but I don't like to inlay that decision into my pension pot.*

Analyst A6 expressed a similar view:

I think yes, there are a few situations [where it could be potentially material]*. One is the emergence of SRI* [socially responsible investment] *type funds and if they became – this isn't our drive to, its not us saying you should be socially responsible or not – if the clients say that they want to run socially responsible funds then we would have to react to that. It's their decision to make and if there was a big drive into socially responsible funds then it would become an increasingly important component of the accounts and what the banks are doing.*

Analyst A12 expressed two viewpoints, beginning with the observation that, 'Well the way things are going ethical investing is really taking off'. He or she continued,

That's a growing phenomenon so there are people in the market that are focusing on these things and if interest in those sorts of issues carries on growing at the rate that it has been then yes I can, in the future, conceive of a time when these sorts of things will be material.

In concluding, however, Analyst A12 said, 'but we're actually a long way off from that now'.

Analyst A1 was asked if he or she could envisage SE disclosure becoming a material disclosure in the future: 'Only if you're running that type of [SRI] fund. Otherwise no, not really.'

The interviewer proceeded to ask Analyst A1, 'So it would need some kind of paradigmatic shift across the whole of the sector for you to be interested in that?' Analyst A1 replied: 'Yes I think so, yes. I'd be interested to see what other people say about that actually. I'm thinking maybe I'm alone.'

Least material part of an annual report
Given the general scepticism of the value of the SE narrative in banks' annual reports each analyst was invited to nominate a section that was the 'least material' to him or her in the conduct of their jobs as analysts.

Analyst A1 spoke for the majority, saying, 'for me as an analyst it would probably be the environmental report'. With a note of sarcasm, Analyst A11 said, 'I'll shock you by saying the corporate social responsibility report'.

Some analysts discussed a situation in which the SE content was not present in the annual report at all. Analyst A14 said: ' No I wouldn't miss it. It would greatly facilitate my reading of the rest of it because it wouldn't be in the way,' and continued to note that it was a section that, 'nobody reads'. Analyst A16 said that: 'It will sound awful but it wouldn't affect me if you lost the whole corporate responsibility section really'.

5.8 'FRONT END' NARRATIVE AS PSYCHOLOGICAL COMFORT

A number of interesting comments were made by analysts in response to an experiment conducted as a part of the interview process, involving the presentation of an annual report with the narrative front end removed from the document. Given that the prevailing view about most of the front end sections was sceptical in terms of value or materiality, the experiment was intended to test the response of analysts to the notional situation where all the developments in narrative reporting were reversed back to a 'technical-only' situation, where the document opened at the auditor's report.

In terms of content that would be missed by analysts by this reversal, the most cited was the divisional or segmental data most frequently disclosed in the operating and financial review (OFR) (or section of similar name). Analyst A1 remarked that, 'you'd miss the divisional... and I'd miss the financial review.' Analyst A5 asked:

Where's the divisional disclosure [in this notional document]*? There is no divisional disclosure. Analysts have pushed incredibly hard over a number of years to get divisional disclosure and people have had to work hard to do it.*

Analyst A7 referred to some of the technical content contained in the OFR:

Things like the additional levels of granularity they give you on things like how they calculate their interest margins, which happens to be one of the key assumptions that we use, in terms of trying to predict the future [would be lost in this notional document].

Analyst A11 said of the annual report without narrative content:

I think I would have lost a significant amount. I would miss the OFR and [expressing a minority view] *I would miss the chairman's statement.*

Opinions were divided over the extent to which, excepting some technical content in the OFR, the narrative content of the annual report would be a serious and material omission as far as the analysts were concerned.

Analyst A1 said that, 'it wouldn't particularly upset me [if the narrative content wasn't there]' but when later asked if it was a comforting pillow to have, answered, 'yes.' Analyst A6 remarked: 'I'm comforted that it's there, yes, definitely. But do I ever use it? Very, very rarely.'

A15 explained the potential effects of the omission of narrative content in a little more detail.

> *Yes, my point is that I think if the front end of the accounts weren't there, despite having a lot of negative things to say about them, I think psychologically it would be a very striking omission in the sense that if there is something that you want to double-check, something that the chairman said or something that the directors are going on about, strategy or whatever it is, it's almost a convenience to have it there for somebody to refer to.* [So] *I like to know that it is there, yes.*

Analyst A16, similarly, expressed the view that despite the narrative content being of little direct materiality in terms of content, its presence in the annual report was a source of reassurance.

> *I think that would be an error of judgement to just take out* [for example] *the risk report even though analysts by and large aren't going to read it. The fact that it's there, you see it's there, you know it's there, gives you some comfort that somebody has thought about it. You look at the risk statement* [for example]. *You presume there's nothing in there so you don't read it. It doesn't mean necessarily you're not valuing it.*

Most of those who expressed the view that the absence of front end narrative would be missed, explained that one of the major objections would be the omission of previously 'taken-for-granted' content.

Analyst A2:

> *When somebody stops disclosing something, then your alarm bells ring automatically. So even if the thing on the face of it is not particularly relevant or you may discount it in the general run of things, if it disappears altogether then that would set alarm bells ringing.*

Interviewer: 'Why so?'

> *I think it's slightly the cynical or questioning nature of an analyst that if something had been excluded then you must be hiding something. There must be some ulterior motive for excluding it and that generally has to be seen as a bad thing.*

Interviewer: 'Would it alarm you if the entire front end was missing?'

> *Yes… even where the statements themselves are quite bland.*

Similarly, Analyst A17 remarked:

> *I think I would* [miss it]. *If it were not there then still you'd probably… say 'hmm'. If it's not there then you would think, 'well what's been going on?' But yes if it wasn't there then actually we would say, 'wait a minute'.*

Analyst A18 said:

> [If the question is] *Is there anything in the front section that I really need,* [then] *the answer is 'no'. But I think you've still got a flavour of the company* [from that content].

Against these views, however, was a substantial body of opinion that the narrative 'front end' would not be missed at all if removed completely.

Analyst A4 was asked, 'would you be concerned if the whole front end was gone?' and replied, 'Not massively'. When asked whether he or she took any comfort from the narrative content being there, Analyst A4 replied, 'No, I don't really, actually'. Analyst A7 was similarly asked whether he or she would miss the front end, if the document opened at the income statement and balance sheet; the reply was, 'From my point of view that would be absolutely fine.' Analyst A10 said: 'I wouldn't miss it at all. So to my mind it is pure waffle.' Analyst A14, when asked whether he or she drew any comfort from the front end, replied, 'None whatsoever'. The interviewer asked whether Analyst A14 thought it would be acceptable if the annual report arrived without the front end. Analyst A14 replied, 'Yes, absolutely'. Analyst A15 said he or she would 'certainly not' have any problems with the whole front end being removed.

6. Discussion

Rather than seeking to provide a range of conclusions and policy recommendations, it is hoped that the evidence provided in this report will assist future researchers in identifying research opportunities and providing them with evidence to enrich existing research findings. In addition to this, however, a number of issues can be raised as a result of the evidence and these fall into the general areas of:

- issues for preparers
- issues for change and analysts' insight.

A final section offers suggestions for further research arising from the findings of this project.

6.1 ISSUES FOR PREPARERS

It is curious, given the substantial growth in narrative content over the years, that little systematic evidence exists for the actual manner in which corporate reporting information is consumed. While part of the volumetric increase can be explained in terms of increased regulation and stock market listing requirements, it remains the case that the vast bulk of the increase is due to enhanced voluntary narrative. Although reporters have bulked out their annual reports with more and more content, little is known either about which audiences consume the respective parts of the annual report or the actual or potential investment materialities of those components.

This study has found, however, that at a fundamental level, the narrative contents of annual reports are relatively unimportant to analysts, who are one of the most important primary consumers of corporate reporting information. There was no consensus among the cohort that any given narrative content category was actually or even potentially material and, in most cases, the majority view was that each section was less than useful. Some sections of narrative reporting were seen by the analysts as being of almost no actual or potential materiality at all.

The most common reasons given by analysts for the assumed immateriality of the relevant disclosures were the lack of numerical content, lack of granularity (both of which affect the usability of the information in a financial forecast) or the assumption that their own clients (the buy-side) were not interested in information based on the type of voluntary narrative in question. The attitudes of the buy-side and their perceptions of sell-side information usefulness were not, however, tested in this research. These issues have been flagged as a suggestion for further research at the conclusion of this report.

So who is all this extra disclosure content actually for? Which audiences are conceived of when the content is being drafted? The content as presented appears, for the most part, to be inadequately detailed to feed into analysts' forecasts although there is some evidence that the contents are used to verify information previously acquired. While some disclosure is insufficiently detailed, other parts are arguably too complex for non-sophisticated users. So it may be the case that some or maybe even most narrative falls 'between two stools' – insufficiently detailed, resolved or granulated for analysts and too complex for non-specialist individual investors.

Some narrative sections were especially poorly thought of by the cohort of analysts. There were very few positive views on the chairman's statement, while the risk narrative was considered largely boiler-plating, and the social and environmental content was universally considered irrelevant. A challenge appears to exist for reporters to take their readers' information needs into greater account when preparing and drafting annual reports.

6.2 ISSUES FOR CHANGE AND ANALYSTS' INSIGHT

Evidence from this study suggests that analysts are very systems-driven and do not often think beyond the narrow confines of their roles in the capital market information 'supply chain'. It appears unlikely that they would be a source of pressure for change in terms of the social or environmental performance of businesses they cover as analysts.

They do, however, claim to be sensitive to the information needs of their own clients in the information supply chain. In this respect, it appears that pressure from the buy-side on such issues as environmental performance may cause a sell-side reappraisal of the materiality and value of social and particularly environmental reporting. It may therefore be that investor pressure on the buy-side for, say, filtration by environmental risk, performance or reporting will present pressure for change in the environmental awareness of analysts. There is a small amount of evidence for pressures of this type in the sell-side/buy-side relationship. The Enhanced Analytics Initiative, for example, is an international collaboration between asset owners and managers aimed at encouraging better investment research, in particular research that takes account of non-financial issues on long-term investment.

Internal change among the sell-side analysts themselves in this respect, however, is unlikely. The technocratic nature of the analysts' skill set renders them less amenable to self-critique. The assumptions of capitalism pertaining to the supremacy of short-term growth and returns pervade the analysts' operational activity.

There may be some grounds for questioning the structural appropriateness of the analysts' skill set in interpreting narrative material for the purposes of financial planning, and in respect of the failure to recognise the potential materiality of secondary environmental risk. While the analysts were quick to dismiss narrative reporting as immaterial owing to its inability to be fed into a forecasting model, a case could be made that notwithstanding the perfunctory nature of much narrative reporting, it is the role of the analyst to interpret narrative content for the purposes of amending numerical forecasting. It is difficult to assess where the balance in this lies between the quality of reporting and the skill of the analyst, but the dismissal of much narrative reporting by analysts may be a de facto admission of an inability to employ narrative content in financial models.

The unwillingness to recognise the possibility of secondary environmental risk may be symptomatic of the short-termism of analysts' financial forecasts. The possibility, at least, has to be admitted that analysts are demonstrating a fiduciary failure to include long-term risk analysis in their reporting, but as criticism of analysts as a cohort is not a purpose of this report this strand of enquiry will be taken no further.

6.3 ISSUES FOR FURTHER RESEARCH

This study has interrogated the user perceptions of annual reports of sell-side analysts, one of the most important (in share allocation terms) audiences of corporate reporting. Given that much of the narrative content of an annual report was considered irrelevant, inadequately resolved and worse ('useless' etc), research opportunities include the interrogation of other user perspectives and analysis of preparer perspectives, especially with regard to narrative reporting.

The cognitive and 'organic' processes involved in the selection of material for, and drafting and editing of, narrative voluntary disclosures remains under-researched. Given that an apparent discontinuity exists between preparers' intentions and user perceptions, research opportunities clearly exist in exploring that. Additionally, if narrative reporting is of little overall use to analysts, research probing the consumption of content by other potential or actual users would be another worthwhile avenue to pursue. Little, for example, is known about the information consumption of small, private investors, non-professional investors and other stakeholders in a reporting company.

In summary, this report suggests a number of worthwhile avenues for further research arising from its findings.

- Further work examining the processes occurring among preparers of voluntary narrative information: in particular, it would be interesting to establish, with a large enough sample, the assumptions of materiality made by preparers with regard to the different categories of voluntary reporting.

- An assessment of buy-side assumptions for the purposes of establishing the extent to which the buy-side need for various information types is met by sell-side reports. In particular, changing attitudes to environmental issues among investors are, given the evidence presented in this report, unlikely to be important to the sell-side but may be more so to buy-side actors.

- The attitudes of sell-side analysts to various voluntary disclosure categories in other industrial sectors, especially the other high volume sectors of oil/gas, pharmaceuticals and technology, where risks and environmental exposures may differ. Similarities found between those and the bank analysts surveyed in this study would emphasise the potential need for change in those areas of voluntary disclosure and any differences could be highlighted for further discussion.

- Studies investigating the manner in which specific voluntary disclosure types are material to investment and to the potential attractiveness of the discloser as an investment. Omissions in material disclosures, perhaps concerning material risks, are one type of failure in this respect while obfuscations and lack of clarity are another.

- A longitudinal study using either qualitative or quantitative research methods to analyse analyst buy/sell recommendations over time and the key factors attributable to changes in recommendations by individual analysts or an analyst group.

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The Future of Financial Reporting 2008: Measurement and Stakeholders

A DISCUSSION PAPER BASED ON THE BRITISH ACCOUNTING ASSOCIATION FINANCIAL ACCOUNTING AND REPORTING SPECIAL INTEREST GROUP (FARSIG) COLLOQUIUM, 11 JANUARY 2008

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The Future of Financial Reporting 2008: Measurement and Stakeholders

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Preface

The Financial Accounting and Reporting Special Interest Group (FARSIG) is a group set up under the aegis of the British Accounting Association. The main purposes of the FARSIG are to further the objectives of the British Accounting Association and for that purpose to encourage research and scholarship in Financial Accounting and Reporting; establish a network of researchers and teachers in Financial Accounting and Reporting; enhance the teaching of Financial Accounting and Reporting; provide support for PhD students in Financial Accounting and Reporting; develop close links with the accounting profession so as to inform policy; publish a newsletter and organise targeted workshops; develop and maintain relationships with the British Accounting Association and the Professional Accountancy Institutes and provide a forum for interaction of ideas among accounting academics.

The symposium, which is one of an annual series, provided a forum for academic, practitioner and policy-orientated debate. Such forums are useful for expressing and developing rounded opinion on the current meta-issues facing financial reporting. They are also useful in that they serve to illustrate the policy relevance of current academic thinking and outputs in accordance with Economic and Social Research Council (ESRC) and The Advanced Institute of Management Research (AIM) calls for relevant and rigorous research through a combination of practitioner and academic perspectives. The importance of the current debate, and in particular that surrounding the issue of the basis of measurement, is further highlighted by a current *European Accounting Review* special edition on 'Measurement Issues in Financial Reporting'.

We would like to express our thanks to all five presenters and their co-authors for their presentations at the symposium and their subsequent time and comments that they provided in the development of this discussion paper. We have tried faithfully to capture the flavour of the original presentations. Nonetheless, although we ran our commentary of the presentations past the original authors, any errors or omissions remain our own. We would also thank ACCA for hosting the symposium and for its support in the publication of the discussion paper. Finally, for any readers who wish to learn more about FARSIG or to become a FARSIG member, please contact either of the authors.

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This paper is available in PDF from http://www.accaglobal.com/publicinterest/activities/library/financial_reporting/other

1. Introduction

Financial accounting and reporting is a curious mix of dynamism and stability. Thinking about the theory and practice of financial accounting and reporting is constantly evolving from generation to generation. Nonetheless, at its core are several key issues that apparently remain eternal, such as a conceptual theory to underpin accounting, how to measure elements within the financial statements and the users of accounting information.

A symposium at the ACCA offices in London, on 11 January 2008, explored some modern views on such perennial topics as conceptual theory, measurement and stakeholders. This report aims to synthesise and provide some informed commentary on the five papers presented at the symposium. These five papers were:

1. *Conceptual Framework: Revisiting the Basics. A Comment on Hicks and the Concept of Income in the Conceptual Framework* (Bromwich, M., Macve, R., and Sunder, S.)

2. *Deciding on Basis of Measurement – Users' Needs or Public Interest?* (Chisman, N.)

3. *Fair Value – An Ongoing Controversy* (Martin, R.)

4. *Fair Value and the IASB/FASB Conceptual Framework Project – An Alternative View* (Whittington, G.)

5. *Communication between Management and Stakeholders: A Case Study* (McInnes, B., Beattie, V. and Pierpoint, J.)

The first four papers addressed a perennial accounting question: how should one measure elements within the accounts? This was addressed from very different perspectives, but all were critical of present measurement practices as encapsulated in current accounting standards. Bromwich et al. challenged current practice from an academic point of view while Chisman drew on his experience as a practising accountant and prior involvement with accounting standards setting to challenge the validity of the 'one size fits all' approach to accounting measurement. He suggested a dual approach based on public and private companies and their differing ownership structures. In the third paper, Martin, head of financial reporting, ACCA, addressed the current and future nature of fair value as a measurement system from the perspective of a professional accountancy body. He showed how the use of fair value had gained in popularity, but also the difficulties in defining and using it and the trade-off between reliability and relevance in accounting measurement and financial statements. The final paper in this area was by Whittington. He provided a thoughtful and reflective critique of the current conceptual framework and measurement debate and then provided an Alternative View counter to the Fair Value View implicitly preferred by IASB.

A particular concern of the papers presented was 'fair value'. There has already been considerable discussion over how to define fair value and how it might be applied. Of the common definitions used within this research SFAS157 is most frequently cited but other relevant sources of fair value use are also referred to, for instance in IAS39,40 and 41.[1]

The joint FASB/IASB conceptual framework review project provides the background and the context against which the seminar and paper presentations can be set. In October 2004, the FASB and IASB added to their agendas a joint project to develop a common conceptual framework building on and converging their own current frameworks, namely the IASB *Framework for the Preparation and Presentation of Financial Statements* and the FASB *Statements of Financial Accounting Concepts*. At a joint IASB/FASB meeting in London in April 2005, *The Conceptual Framework – Objectives of Financial Reporting* was outlined. This related to the convergence of the respective frameworks and reporting standards. It covered, inter alia, the objectives of financial reporting, the roles of decision-usefulness and stewardship, and the range of users of financial statements. Additional detail is provided in a FASB/IASB paper of May 2005, *A New Conceptual Framework Project* by H. G. Bullen (FASB senior project manager) and K. Crook (IASB senior project manager). The overall joint conceptual framework project is being undertaken in phases and comprises the following.

- Objectives and qualitative characteristics.
- Elements and recognition.
- Measurement.
- Reporting entity.
- Presentation and disclosure.
- Framework purpose and status.
- Application to not-for-profit entities.
- Remaining issues.

The papers presented at the symposium primarily contribute to the first three of these main areas as well as more generally to the debate on the conceptual framework. They provide an informed critical review from academic, practitioner and policy-orientated perspectives. The papers address areas central to this debate and provide reflection on issues of the foundation of past, present and future measurement bases within financial statements, the trade-off between relevance and reliability (now replaced by faithful representation), the role of stewardship and decision-usefulness, and the underpinning market assumptions upon which the conceptual framework is constructed.

1. For a more in depth debate concerning fair value and its meaning as defined by IASB see Alexander (2007) '*A Recent History of Fair Value*' and more generally Walton (2007).

The first joint IASB/FASB discussion paper on the conceptual framework was published in July 2006, and set out the preliminary views of the IASB and FASB on the objectives of financial reporting and the qualities that make the information useful for decision making. The importance of the debate was highlighted by Ian Mackintosh, ASB chairman, who stated:

'While many may think of the conceptual framework project as simply an academic subject far removed from the practical day-to-day world of accounting, that is not the case. The framework will have far-reaching practical implications in influencing the future direction of financial reporting. The ASB believes that it is important that all constituents are made aware of the proposals and their implications and we will be playing an active role in the debate on these issues' (see www.iasplus.com/uk/0607frameworkasbpr.pdf).

It is against such sentiment that the symposium provided a forum for critical discussion of the current issues within the conceptual framework project and for the future orientation of financial reporting. An up-to-date review of the continuing development of the joint conceptual framework and its phases is available at http://www.fasb.org/project/conceptual_framework.shtml

The debate concerning measurement is timely and contextualised against the current global financial situation. The US Federal Reserve chairman, Ben Bernanke, sees mark-to-market or fair value accounting as contributing to the destabilisation of the financial markets due to the write down of distressed assets to fire sale prices (reported, April 2008). He views fair value as more appropriate in times of financial stability and calm. Further, the initial rejection by the US House of Representatives of the proposed US Paulson bail-out plan for the financial markets also raised the issue of calls for stricter rules on accounting practices and measurement away from mark-to-market accounting. Against these current challenges to mark to market, there is strong support for its continued use. The Council of Institutional Investors, which manages more than $3 trillion-worth of pension assets, opposed the rescinding of mark-to-market accounting. Both regulators at the Securities and Exchange Commission (SEC) and standard setters at the Financial Accounting Standards Board (FASB) are working on additional guidance for mark-to-market accounting at the time of writing (October, 2008, see Financial News Online, 1 October 2008). In the UK, Michael Izza, chief executive of the Institute of Chartered Accountants in England and Wales, has also highlighted the wider public importance of the current debate on mark-to-market accounting, when speaking on Radio 4, 2 October 2008. The impact of the current financial turmoil and the needs of financial markets are also evident within recent IASB/FASB announcements with Robert Herz, chairman of FASB, stating 'we will continue our dual objectives of working toward global convergence while addressing reporting issues of critical importance to *US investors and financial markets*' (emphasis added by authors, 11 September 2008 IASB/FASB press release).

The fifth paper, by McInnes, Beattie and Pierpoint provided an academic perspective on another accounting issue of continuing interest: stakeholder communication. The study adopted a multi-stakeholder group perspective to examine a wide range of information sources and their levels of uptake.

These five papers thus provide new insights into old topics. For the topics of a conceptual framework, accounting measurement and stakeholders have been addressed for many decades, if not centuries. For example, Edwards, J.R. in *A History of Financial Accounting* (1989), outlines the continuing debate over what constitutes accounting measurement throughout the nineteenth and twentieth centuries and before.

Edwards focuses on the historical development of accounting practice, emphasising the need to understand the legal, economic and social context in which such changes occur. 'Since then [the mid-nineteenth century] there has been a change in emphasis from record keeping to financial reporting and, as regards the functions of those reports, from using them as a means of assessing stewardship to their use as the basis for resource allocation decisions' (Edwards 1989: 15).

Initial attempts at profit measurement were crude and often haphazard and in many businesses the owner would assess profit on the cash reserves that could be drawn from the business. Throughout the industrial revolution the main item of significance for businesses was the amount spent on machinery and consequently attention was drawn foremost to the measurement of fixed assets. In general terms, however, 'the absence of a general agreement about which profit measurement and asset valuation procedures should be used provided ample scope for nineteenth-century managers to prepare reports designed to meet managerial objectives rather than to portray fairly the underlying economic facts' (Edwards 1989: 125). Until the development of accounting and legal regulations in the period after the Second World War, with Technical Advisory Committee recommendations (1942–69) and successive Companies Acts governing financial reporting, there was 'considerable variation in the treatment of published items of income, expenditure and appropriations to profit (Edwards 1989: 130). Thus the measurement debate is not new, although the arguments within it may have become more sophisticated.

The current debate on the conceptual framework, measurement and stakeholders can probably be traced back to at least the 1970s. Taking the UK as an illustrative example over the past generation, there has been a succession of pronouncements on a conceptual framework and on measurement. These include:

1971 ASC, *SSAP2 – Disclosure of Accounting Policies*

1975 ASSC, *The Corporate Report*

1975 Sandilands, F., *Inflation Accounting: Report of the Inflation Accounting Committee*

1981 Macve, R., *A Conceptual Framework for Financial Accounting and Reporting: The Possibilities for an Agreed Structure* (ASC)

1988 ICAS, *Making Corporate Reports Valuable*

1989 Solomons, D., *Guidelines for Financial Reporting Standards* (ICAEW)

1991 Arnold, J. et al., *The Future Shape of Financial Reports* (ICAEW/ICAS)

1999 ASB, *Statement of Principles for Financial Reporting*

Possibly the most influential, as it set the scene, was *The Corporate Report*, which was issued as a discussion paper by the ASSC (1975). It raised questions over the aims and quality of financial reporting and to whom such reporting was addressed and marked the 'first real attempt by the accounting profession in the UK to develop a conceptual framework' (Ernst and Young 2001: 106). It sought to identify user groups for financial accounts and their respective information needs for making decisions. Two user groups, shareholders and creditors, and five additional groups were identified, namely employees, government, financial analysts, the business contact group and the general public. The issue was how financial reporting could address the sometimes-conflicting needs of these groups and the need for greater disclosure. Measurement issues, such as the inadequacies of historic cost, were discussed as part of the paper.

The Corporate Report itself was overtaken by events with the publication of the Sandilands Report (1975) on Inflation Accounting, which explored current purchasing power, current value accounting and cash flow accounting as measurement systems. After this there were a succession of reports such as the Macve Report (1981, reprinted in Macve 1997), *Making Corporate Reports Valuable* (MCRV) (1988), *The Future Shape of Financial Reports* (Arnold et al. 1991) and the Solomons Report (1989), all of which grappled with conceptual and measurement issues.

Finally, the *Statement of Principles for Financial Reporting* was issued in 1999 by the ASB; this stemmed from a 1995 exposure draft that had adopted a balance sheet focus. The original exposure draft was widely criticised for its position on the move to current values and the recognition of gains/losses in the profit and loss account or the proposed Statement of Total Recognised Gains. The final publication in 1999 contained eight chapters. These chapters continued to grapple with the issues raised in *The Corporate Report* (ASSC 1975) (and, indeed, those in the current IASB/FASB Conceptual Theory documents). These issues included the objective of financial statements; the qualitative characteristics of financial information; the elements of financial statements; recognition in financial statements; and measurement in financial statements. These issues were widely addressed and critically discussed by our presenters as set out in Chapter 2 below.

The remainder of this research report can be divided into three chapters. In the next chapter, we outline the five papers that were presented. Then, in the Discussion chapter, we attempt to synthesise some commonalities and discontinuities in approach between the authors. Finally, in the Conclusion we summarise and suggest some ideas for future development.

2. Symposium Papers

2.1 CONCEPTUAL FRAMEWORK: REVISITING THE BASICS. A COMMENT ON HICKS AND THE CONCEPT OF INCOME IN THE CONCEPTUAL FRAMEWORK. MICHAEL BROMWICH, RICHARD MACVE AND SHYAM SUNDER[2]

This paper, which was presented by Richard Macve, critically examines the FASB/IASB project on the conceptual framework; its assertion of the primacy of the 'asset/liability' approach to income against the 'matching' of revenues and expenses approach; and its claimed underpinning by Hicks's definition of income. The FASB/IASB (2005) paper *Revisiting the Concepts* lays down the approach that a concept of income founded ultimately on the definition of assets is necessary because, among the proponents of the alternative revenue and expense view, none could meet the challenge of defining income directly without reference to assets or liabilities or recourse to highly subjective terminology (like proper 'matching'). As the Boards' definition of liabilities is derived from that for assets, the conceptual primacy of assets has become the bedrock of the Boards' frameworks and it is claimed that such primacy is derived from Hicks's definition of income (1946).

Macve et al. critique this 'bedrock'[3] and argue that Hicks's concept has been misquoted and, therefore, misunderstood and misapplied. They review some alternative approaches and conclude by challenging the Boards' view that accounting 'conventions' need replacing by 'conceptual principles' within the Conceptual Framework Review. Their paper argues that accounting concepts and conventions must be seen as complementary rather than as standing in opposition to one another.

According to FASB/IASB the overriding objective of financial statements is their usefulness in making economic decisions by giving assistance in predicting future cash flows.[4] The Boards' focus is on 'enterprise resources, claims to those resources and changes in them'; a focus which leads to and is consistent with their definitions of elements within the financial statements. In this, assets are characterised as 'probable future economic benefits obtained or controlled...as the result of past transactions'. As all other elements can be derived from assets, they have conceptual primacy and this supports the superiority of the asset/liability view of income against the revenue/expense approach. Income is the increase in net resources in terms of increases in assets and decreases in liabilities and can be objectively determined from the change in the entity's wealth plus what is consumed during a period. Further, it is claimed that the definition of assets does not encompass the 'deferred debits' that result from a revenue/expense or matching approach to measuring income. Nonetheless, as it has long been recognised in traditional accounting texts that 'deferred revenue expenditure' is only carried forward in line with the economic benefits that are expected to accrue in future years, Macve et al. argue that this is effectively equivalent to the Boards' definition of 'assets'.

The Boards cite Hicks (1946) in support of the objectivity of the 'primacy of assets' view of income. Macve examined in detail how Hicks (1946) has been taken out of context and misapplied, so that reliance on his support is invalid. As a consequence, this undermines the whole basis of the 'primacy of assets' approach.

The differences between what Hicks actually argued and what the Boards' 2005 paper claims he said are summarised in Figure 1.

Figure 1: Implications of FASB/IASB's vs Hicks's view of 'income'

IASB/FASB	Hicks
'Net assets'	Firms[5]
'Objective'	Largely subjective
Income ex post	Income ex ante[6]
Income 'No. 1'	Income 'No. 2'[7]

2. The full working paper is available at http://www.lse.ac.uk/collections/accounting/facultyAndStaff/profiles/macve.htm

3. '...a wise man, which built his house upon a rock...a foolish man, which built his house upon the sand...and it fell; and great was the fall of it.' *Matthew*, 7: 24-27.

4. The 'stewardship', 'contractual' and other functions of accounts are not explored further here. Whittington (2008) deals with them in detail.

5. Developed in Hicks (1979) as 'proprietors'

6. cf. Hicks (1948)

7. Or 'No.3' (Hicks, 1946): cf. Paish (1940)

The paper reviews each of these significant differences in turn.

i. 'Net assets' or 'firms'?

Hicks (1946) discussion is about individuals' income. In a later paper (1979), he examines firms' income but conceptualises this as the income of the owners of the firm (collectively) not by considering the firms' assets and liabilities. There is no justification for FASB/IASB regarding Hicks's 'capital value' as being fully captured in the firm's assets and liabilities.

ii. 'Objective' or 'subjective'?

Hicks (1946) regards 'income' or 'profit' as representing how much can be (safely) taken out of the business. This estimated profitability is a matter of judgement, but such use of judgement may cause disparity of opinion between parties connected to the business—the owner against tax authorities for instance—and so profit cannot be measured in that way for practical purposes. Bringing in the need for fixed asset depreciation and overhead allocation further emphasises the accounting and economic judgements that have to be made, clouding the issue further as to the maximum (profit) that can be safely taken out of the business.

FASB/IASB (2005) quotes Hicks (1946) as saying that 'Income No 1 ex post is objective'. In fact, the full relevant sentence reads 'so long as we confine our attention to income from property,[8] and leave out of account any increment or decrement in the value of prospects due to changes in people's own earning power... Income No.1 ex post is not...subjective;...it is almost completely objective'. Nonetheless, as markets are not complete or perfect there will be a large element of the value of future cash flows that is not captured in the value of current net assets ('property'). This value, which derives from the quality of the management of those assets within the business, is what Hicks (1946) labels 'Human Capital'. So the only objective ex post measure of business income would be the change in capital value at the stock market rather than entity net assets level (ie changes in the value of market capitalisation and dividend). This makes financial reporting to shareholders of the firm's activities and net assets redundant.

iii. 'Ex post' or 'ex ante'?

Ex ante income reflects what is expected about future cash flows (which must be subjective) and ex post what has actually happened to cash flows during the period, together with revisions to expectations of the future at the period end (which could be objective only under the restricted conditions discussed above). Hicks (1946) argues that ex post calculations have no significance for conduct and no relevance to decision-usefulness, but instead form part of economic and statistical history. For FASB/IASB's 'asset primacy' to be a bedrock then it surely must satisfy the basic criterion of decision-usefulness, the primary purpose of financial statements: so reliance on Hicks's ex post concept of income (1946) must fail this test.

iv, 'No. 1' or 'No.2'?

Hicks's 'Income No. 1' (1946) is equivalent to the maximum amount that could be distributed to shareholders in a period while leaving intact the firm's initial capital value. When interest rates change, however, this is not the same as the maximum amount that could be distributed so as to leave intact the ability to distribute the same amount in future, which is Hicks's 'Income No. 2'.

Disclosure of such 'permanent' or 'standard income' would provide future decision making usefulness. Given that income stream and an appropriate discount rate, a market value for the firm can be calculated. Indeed, companies themselves now often report levels of permanent or maintainable income. Macve et al. use AstraZeneca's 'Business Highlights' section of its interim report for the half year ended 30 June 2007 (17) as an example of such reporting: 'Management believes that investors' understanding of the Company's performance is enhanced by the disclosure of core EPS, as it provides understanding of the underlying ability to generate returns to shareholders'. So for quoted companies Income No.2 would relate to the maximum maintainable level of dividends that can be paid in the current and all future periods. Macve et al. contend that given such maintainable income (and its practice-based disclosures), under further restrictive assumptions, assets and liabilities can be derived from it, not it (income) from them (net assets). This is consistent with Ohlson (2006), who argues that reporting such maintainable earnings, as a starting point for investors' future decision making, would require that assets and liabilities be derived from income and not vice versa: so the alleged superiority of the assets approach to income is dismissed.

When Hicks in full is considered, there is no justification for regarding 'capital value' as fully captured in assets and liabilities. The debate continues as to how far the concepts and alternative measures of asset and liability values are consistent with Hicks's capital value and how changes in net assets can be related to Hicks's Income No. 1, and what assumptions are necessary to accommodate this.

If any measure of income is relevant for decision making it must be ex ante income, which is necessarily subjective. Historic, ex post income, can, however, help predict the future ex ante income and gives importance to the underlying statistics that accounts record. To serve this purpose accounts should contain the maximum of information within the prescribed limits. The main issue with ex post income is how much it helps in forming expectations about future income ex ante and therefore fulfils the decision-usefulness criterion. This depends, inter alia, upon the permanent elements of income as against the transitory ones, and their ability to be differentiated. While accounting conventions themselves can be improved upon, the purpose of accounting information is to facilitate decision making and decision makers themselves are

8. That is, exchangeable assets for which everyone faces the same prices (eg Beaver and Demski, 1979)

probably most able, and best placed, to make appropriate adjustments, as they see fit, to an underlying statistical record (Brief 1982).

Hicks's (1946) Income No. 1 is concerned with capital value changes, Income No. 2 with maintainable income. The relevant income concept to use will bring more insight into the assets/liabilities versus income/expenses debate, as to the most useful approach to measuring enterprise income.

The final part of the paper questions the Board's pitting of 'conventions' against 'conceptual principles'. It is noted that FASB/IASB (2005) views the Conceptual Framework Project as a crusade against conventions, arguing that standards should be rooted in fundamental concepts rather then a collection of conventions. In their presentation paper, Macve et al. argue that this is a false opposition. Conventions are necessary social constructions and the role of concepts is to question whether, why and how conventions need changing or replacing and whether, by doing so, better decision making would result. To rewrite a key sentence from page 1 of the FASB/IASB (2005) paper: 'To be principles-based, standards have to be a collection of (socially) useful conventions, rooted in fundamental concepts'. It is therefore important that the FASB/IASB Project 'revisits the concepts' in a much more fundamental way if it is to base the conclusions on solid foundations.

2.2 DECIDING ON BASIS OF MEASUREMENT – USERS' NEEDS OR PUBLIC INTEREST? NEIL CHISMAN

This presentation provided practitioner-based insight and discussion into the current and future bases of accounting measurement. Neil Chisman outlined current measurement bases, before turning to issues of company size and ownership and the purpose of accounting information to address the needs of stakeholders. The presentation provided a critique of accounting bases and moved on to discuss the validity of a dual basis for measurement, compared with the current mixed measurement approach or a single measurement basis.

Four main and commonly used bases of accounting measurement were outlined:

- recoverable historic cost (RHC) – lower of cost or net realisable value
- fair value – defined by SFAS157 as 'the price that would be received for an asset or liability in a transaction between market participants'
- value in use – the net present value of future cash flows
- mixed basis – combinations of the above for different balance sheet items.

Currently, a mixed basis is used when preparing accounts, giving rise to the anomaly that different bases of measurement are used within the financial statements rather than a single unified measurement basis, which would facilitate simpler and more coherent accounting and accounting standards. The first issue that needs addressing is the underlying purpose of financial statements and then from that there is a need to adopt a suitable basis of measurement. Too often the debate over accounting standards has revolved around the size of an entity and the differences between large and small companies, but the real issue to be addressed is that of ownership, as there are clear principles associated with ownership that can then be used to provide a framework for an appropriate basis of measurement. Public and private companies have different ownership structures, giving rise to different purposes and needs for their financial statements, and accordingly these should be considered separately. If the very purpose of accounting is different for public and private companies why should the basis of measurement be necessarily the same?

One common purpose of accounts for all companies is creditor protection, i.e. allowing creditors to assess the financial viability of the business. For public companies, a second fundamental purpose is for investor protection (arising from agency costs), but for private companies where the shareholders and the directors are common, this is not the case. For private companies, the basis of measurement needs to ensure appropriate creditor protection and then beyond that to be simple and not burdensome so that the owners of the business can concentrate on their business and not on complex accounting issues. By adopting RHC the simplest accounting basis would be used, clearly showing a prudent net assets position of the business and so satisfying the need of basic creditor protection. In essence: 'Little GAAP is RHC accounting'. Nonetheless, there are some small companies that have shareholders who are not directors and this raises the issue of appropriate investor protection as well as the now-resolved creditor protection. A solution to this is two-fold. If all the shareholders are happy with RHC as a basis for measurement then that can be adopted; alternatively, if they are not happy with RHC then the company would need to follow the 'Big GAAP' rules that apply to public companies and are designed with investor protection as a key consideration. It may also be that many larger private companies would also adopt 'Big GAAP' rules, but that would be decided on by the shareholders.

For public companies, the financial statements need to satisfy creditor and investor protection requirements and, consequently, the appropriate basis of measurement is that which reflects the rationale of shareholder value creation and the overall value of the business, as well as protecting creditors. Another issue emerges at this point, namely the general lack of consensus, as well as biased personal motivations, between financial stakeholders and shareholders in public companies over the format of financial reporting and their respective needs. To find common ground, the question of the fundamental purpose of public company accounts really needs to be resolved. First, to enable investors (users) to make buy/sell/hold decisions, and second, to decide if management intervention is needed owing to poor performance. Both these types of decision require cash flow forecasts and a company valuation, which will also focus the company (and its investors) on value creation. At present, users do not have sufficient information on which to base decisions and rely on sketchy valuations, management meetings and their own forecasts. Potential consequences of this are sub-optimal decision making, unclear performance objectives and associated underperformance, and a focus on short-term profit rather than longer-term value creation. Financial statements that reflect value creation and clear reporting are needed to enable optimal shareholder decision making. Nonetheless, while forecasts and valuations would be welcomed to satisfy this objective, they remain estimates and lack the reliable objective factual information that RHC provides.

Looking at the balance sheet, the single most important item is 'fixed assets', both in value terms and also in their use in enabling the business to operate. By combining fixed assets within the business, 'cash generating units' are created and these in turn comprise business segments that then make up the overall business. In determining a fixed asset purchase, net present value and forecasts are used by management to justify the decision and assess its impact on long-term value for the business. Fixed assets and their accounting need to be understood, rather than current net assets, whose values are more readily determined as they revolve around operating transactions.

In this presentation, each of the bases of measurement was then considered in relation to fixed asset accounting and the need to satisfy investor protection and the focus on value creation.

Recoverable historic cost (RHC)

RHC is well understood and is the traditional measurement basis for recording fixed assets at cost and then reducing them by an appropriate depreciation charge over their useful economic life. The cost is reliable and although depreciation is based on a management estimate, it is not complex and is viewed as prudent valuation. Nonetheless, it relies on cost as the prime driver of measurement rather than any earnings potential for which fixed assets are purchased for, thus its direct relevance as a measurement basis is very limited in terms of investor needs.

Fair value

As outlined in SFAS157, fair value has good application to traded assets such as financial instruments (options) and can be applied to some fixed assets such as real estate, hotels and pub chains. The crux with fair value is that the value is derived from the sale of those assets in the market. This means that for fixed assets, which may be unique to a company and therefore not readily benchmarked with similar assets, the value would only come from their sale to another party. By implication those assets are now no longer part of the original business nor generating income under the original businesses' management and knowledge. So the fair value of fixed assets would relate to their future cash flows after sale rather than their future cash flows within the current business. This presents considerable measurement and estimation problems, based on the use of the fixed assets and the management of them within a new business, and appears almost untenable as a basis of measurement. The concept is that of winding-up value rather than investment value. It may be better applied in a winding-up situation, where any value can be based on the assets' future use rather than its written down historic cost. The purpose of this debate is, however, to obtain a suitable measurement basis for continuing businesses rather than failed ones.

Value in use

Value in use is the basis that represents the investment value. It uses discounted cash flow analysis based on forecasts of future cash flows from the fixed assets as part of their cash generating unit within the business. The forecasts could be presented with sufficient supporting disclosures around management assumptions so enabling investors to focus on value and management performance rather than having to create their forecasts from historically based accounts. Nonetheless, the forecasts are not facts and may be skewed by management. So how can such forecasts and the underpinning assumptions be made more reliable and acceptable to enable value in use to be considered as a basis for measurement? First, it can be done by greater disclosure of forecast information, which is currently produced for internal use but not disclosed, although cash flow forecasts are disclosed to debt rating agencies (see McInnes et al. 2007). Forecasts are also used as the basis for prospectuses. Secondly, it can be done by disclosure of the management assumptions on which the forecasts are based and their rationale, which could include, inter alia, strategic fit and risk assessment. This gives a framework for companies to tell investors about their future value creation and their strategy. Forecasts and assumptions would then be used to monitor future performance by focusing on value creation and the ability to meet forecast levels so fostering the need to make credible and achievable forecasts. This approach would also steer future buy/sell/hold decisions and management intervention on the basis of any future underperformance. It remains true, however, that reliance is on estimates rather than on recorded fact.

The issue is then a trade off between forecast information that would facilitate focus on value versus factual historic information that does not focus on future value. To adopt a single basis of measurement results in deciding between the two choices of RHC and value in use. An alternative is to consider both bases in parallel rather than to apply one basis to some areas of the balance sheet and another basis to others, as currently happens. No single basis is satisfactory on its own so therefore a Dual Basis is proposed. The accounts would report all items under RHC (the same as Little GAAP discussed earlier) to give objective reliability, and would then report under 'value in use' to provide forecast and value-driven information. To achieve this, two formats could be followed, either by giving separate RHC and value in use statements or by adding a bottom half to the profit and loss account and balance sheet so that the bottom line gives the investment value information. The balance sheet would be the statement of company value, and the profit and loss account the statement of value creation.

The dual basis for public companies and those private companies that require more than just RHC meets all requirements. There is a factual basis of measurement (RHC) providing appropriate creditor protection and there is a forecast and value-driven basis of measurement from value in use, providing appropriate protection and information for investors. Rather than having to produce second-hand forecasts based on historic information, investors and analysts could now focus on management forecasts and their assumptions. This means that public companies focus on value creation while at the same time, through RHC, they provide appropriate creditor protection. Private companies not requiring any more than RHC (little GAAP), which addresses creditor protection, are able to focus on their business objectives without worrying about complex accounting issues and associated time-consuming bureaucracy.

A clear distinction is now possible, based on ownership: itself a factual base. For private companies there is straightforward RHC. If necessary, as determined by the shareholders, private companies can also adopt the dual basis. The dual basis would be applied to all public companies. The dialogue between managers and investors becomes more focused on value, underperformance is easier to identify, and investor time is spent more effectively, analysing real company forecasts and their underlying assumptions. Whether this becomes reality and is applied in the future is another debate for all accounting bodies and stakeholders.

2.3 FAIR VALUE – AN ONGOING CONTROVERSY, RICHARD MARTIN

Richard Martin, head of financial reporting at ACCA, examined the present and future for fair value reporting. Owing to the problems of measuring cost and the number of potential bases of measurement, fair value is a means of providing values/costs for assets and liabilities. Nonetheless, it is not problem free, for instance there are issues concerning market measurement, reliability and the role of provisions. Fair value has been applied to intangible assets, investment properties, derivatives and financial instruments, both traded and non-traded. While historic costs remain a permanent record with appropriate amortisation or depreciation charged to reflect the use of the asset, fair values will change over time. These changes in fair value affect profit for the year. Appropriate accounting standards already exist in specific areas (for instance, IAS39 for Derivatives and Traded Financial Instruments; IAS40 for Investment Properties; and IAS41 for Agriculture). A similar change in value occurs through asset revaluations such as those for fixed and intangible assets.

Because extant accounting standards now use a fair value approach, fair value has become a mainstream basis of measurement, giving us the possibility of fair value accounting. This is further evidenced in the Business Combinations Revision and Insurance Contracts – Part 2. The overriding consideration is how to consistently ascribe fair value to all items and to answer the posed question of 'what exactly is fair value?' This is substantially dealt with in the proposals of SFAS157 and the proposals in the IASB (2006) discussion paper giving a more precise meaning and instances of application. Fair value is an exit value for the owner as a market participant, recording the transaction price and the fair value of assets and liabilities. Under SFAS157, there are three levels for determining fair value: Level 1 for quoted prices in an active market; Level 2 for observable information other than in an active market; and Level 3 where no observable market data exist. There is thus a hierarchy of values: market prices, comparable prices, and unobservable inputs. The fair value hierarchy is inherent in the application of IAS39. For derivatives traded or held in an active market, there exists a quoted daily price where the relevant bid price is used but no extra value is recorded for a large block holding even though it is potentially material. Where there is no active market, a valuation model is applied using all relevant factors that affect valuation, including time to maturity, credit risk, volatility of market and underlying asset, liquidity risk.

Using this framework, can fair value be applied to more items rather than to more specific categories such as derivatives or investments? There are very different views on this, with its most ardent supporters arguing that fair value is the only information relevant to financial decision making and thus as such should be fully adopted to satisfy decision-usefulness. The Canadian Discussion Paper favoured fair value and the proposed measurement hierarchy would follow in the order fair value, current cost and lastly historical cost. The advantage of fair value is that it is able to capture more information that is also relevant for future decision making. It is market-specific, not entity-specific, and so captures a consistent market value of items. By using fair values all assets and liabilities are recorded and recognised consistently so adopting a common treatment and not separated by the issue of their historic purchase price. It is their value within the business that should be measured and not the price at which they were purchased. Market rather than entity valuations are more objective and so enable greater comparability between businesses and enable comparison for future decision making rather than transactional past decisions.

Nonetheless, fair value is also, like any of the competing measurement bases, subject to a number of weaknesses and criticisms. It results in volatility of asset and liability measurement. By moving away from a transactions base, there is an early recognition of gains (rather than a more conservative approach) and, while relevant for future decision making, it may not be reliable. Furthermore, it is more costly for all businesses to apply and, for some elements, current fair value is difficult to ascribe and thus reliability, rather than relevance, becomes a concern. Issues of reliability are material in the light of Enron, the subprime crisis and recognition of insurance liabilities, but is there too much subjectivity once you move away from market values?

The conceptual framework's objective is to achieve a reporting that is an honest record of recent performance. This will facilitate future cash flow prediction and consequently business valuation. The best thinking of the time is incorporated into current accounting standards, and assets and liabilities are dealt with properly, although this means a mixed basis of measurement. To reduce the complexity, a single basis of measurement needs to be considered, but one basis may not present a uniform solution to all of the issues. Historic cost is the default basis for many operating assets and liabilities; fair value (current market exit value) is useful for traded financial instruments and derivatives; and value in use has potential for future cash flows for provisions, insurance and trade receivables. A key question for fair value, is whether the reporting of fair value changes can be simplified, as even based on existing treatments, there are problems with areas such as associates and joint ventures, deferred taxation and hedge accounting.

At present there exist a variety of measurement bases and consequent different treatment of items within financial statements. There has been a growth of fair value accounting in more recent accounting standards and a detailed recognition of fair value in SFAS157. The trade off between reliability and relevance is an issue facing all bases of measurement, but greater understanding and clarity is needed for reliability and the need for relevance within financial statements should be recognised. Fair value can be more supported with greater consistency of application and precision of meaning that may contribute to an eventual reduction in accounting complexity towards a single, unified, measurement base. To support this, a revised conceptual framework, with fair value as an adopted basis of measurement, may be required.

2.4 FAIR VALUE AND THE IASB/FASB CONCEPTUAL FRAMEWORK PROJECT – AN ALTERNATIVE VIEW, GEOFFREY WHITTINGTON

Geoffrey Whittington's presentation outlined and discussed the issues arising from the IASB/FASB's project to develop a joint conceptual framework for financial reporting standards, in particular the implications for the basis of measurement. He articulated two 'world views' underlying the current framework and measurement debate: A 'Fair Value View',as the perceived preference of the IASB, and an 'Alternative View'. Each of the world views were illustrated with reference to specific standards and their practical implications. The presentation concluded with a summary of the respective 'world views' and implications for some IASB proposals affected by the 'Alternative View'. Interested readers are urged to read Geoffrey's full paper which is published in *Abacus*, Volume 44, Number 2, June 2008, pages 139–68.

Fair value as the basis of measurement is the perceived preference of the IASB. Two papers issued (but not necessarily endorsed) by the IASB discussed fair value as the basis of measurement. They were a discussion paper in 2005, authored by staff at the Canadian ASB, and FASB's SFAS157 in 2006, which interpreted fair value as being current market sale price, ignoring transaction costs and free of entity-specific assumptions. The Fair Value View is based on the assumption that markets are relatively perfect and that financial reporting should meet the needs of passive investors and creditors (the focal group for establishing needs) by reporting fair value derived from current market prices. The Fair Value View emphasises decision-usefulness and relevance to current and prospective investors and creditors (not just present shareholders) with the focus on forecasting future cash flows so that accounting information ideally reflects future, rather than past, transactions.

The 'Alternative View' is the collective term used for a world view that is based upon a different set of assumptions from the Fair Value View. It implicitly encapsulates criticisms of the IASB fair value based pronouncements. The 'Alternative View' embraces the whole framework, including measurement, and is based on the assumption that markets are relatively imperfect, so that reliability matters, and that in such a setting financial reports must meet the needs of current shareholders as proprietors, and therefore explicitly recognise the importance of stewardship. Present shareholders have a special status and stewardship is equally as important as decision-usefulness. Financial reporting entails reporting past transactions and events using entity-specific measurements that reflect the opportunities actually available to the reporting entity. Moreover, past transactions and events are important for both stewardship and as an input to help predict future cash flows.

The IASB/FASB Joint Conceptual Framework Project started in 2005 with two objectives. A primary objective was to converge the two conceptual frameworks to form a consistent base for the convergence of financial reporting standards. Both IASB and FASB frameworks already emphasised decision-usefulness as the primary focus of financial reporting, as opposed to legal and stewardship purposes. The second objective was to make improvements, for instance by filling gaps, such as critical guidance on measurement, and to provide greater consistency, such as the definition of a liability and the distinction between liabilities and equity. A series of discussion papers followed by exposure drafts have been and will be issued as part of the project timetable. The first discussion paper (Phase A) was published in July 2006 entitled, 'The Objectives of Financial Reporting and Qualitative Characteristics of Decision-Useful Financial Reporting' and this was discussed in detail in Geoffrey Whittington's presentation as outlined below. Subsequent discussion papers (Phases B to H) covering Elements and Recognition, Measurement, Reporting Entity, Presentation and Disclosure Framework, Purpose and Status, Application to Not-for-profit Entities and Remaining Issues are to be issued from 2007/8 onwards.

Chapter 1[9] of the discussion paper is on the 'Objective of Financial Reporting' and this is fundamental to the Framework debate. This reiterated the need to produce 'general purpose financial statements' to meet the needs of all external users, with investors and creditors as the focal group. This is consistent with the current conceptual framework and implies a focus on valuation by financial markets.

What of the special role of present shareholders as proprietors of the business and the issues of stewardship, agency tensions and accountability? Any special role for current shareholders is rejected by the discussion paper on the grounds that a 'broad' entity perspective is more inclusive than a 'narrow' proprietary perspective and any stewardship obligation within reporting requirements could be subsumed within the general objective of decision-useful information derived from future cash flows. Thus stewardship is not specified as a distinct objective of financial reporting in the discussion paper.

The 'Alternative View' rejects the subsuming of stewardship in this way. Under this view, accountability and the needs of the present shareholders entail more than the prediction of future cash flows, as they are concerned with monitoring the past as well as predicting the future. The Alternative View also recognises that the past and future are interlinked and overlap. For example, information (and monitoring) on past transactions and events and the past conduct of management and policies may be relevant to predicting future cash flows. The stewardship process can affect behaviour and therefore

9. Since the talk was given (January 2008), the IASB has issued revised versions of Chapters 1 and 2 as an Exposure Draft (May 2008)

influence future cash flows and their perceived risk. By explicitly recognising stewardship as an objective of financial reporting, agency concerns and accountability issues are more fully addressed. The differences between the two objectives of decision-usefulness and stewardship is more one of emphasis, but the 'Alternative View' recognises the distinct role of stewardship, which is not subsumed within the single objective of decision-usefulness.

Chapter 2, 'Qualitative Characteristics of Decision-Useful Financial Information' was discussed next. As expressed in its title, it is based on the general objective of decision-usefulness for financial reporting, with stewardship subsumed. Additionally, there are changes to both the form and language used in the existing conceptual frameworks. With regard to form, a sequential rather than the previous simultaneous approach (in which trade-offs were made) to applying the qualitative characteristics is advocated. For language, there is the replacement of reliability with faithful representation. The combined effect is to eliminate the trade-off that previously occurred between relevance and reliability. Such a trade-off was previously used under the present framework as a reason not to use fair value measurements, because these were perceived to be relevant but not reliable. Under the proposed new Framework (supportive of a Fair Value View), relevance is to be considered first followed by faithful representation. There are, however, different levels of relevance and faithful representation, which give rise to trade-offs between them. As relevance is considered first, this will prevail, despite the potential problems and issues of unreliability. An increase in reliability is thus not regarded as a factor to outweigh relevance. The change to faithful representation can also be seen to be supporting a 'Fair Value' view. Information must be a faithful representation of real-world economic phenomena depicting the economic substance of the underlying transaction or event – and it must be verifiable, neutral and complete, which may serve to emphasise economic substance over accuracy (see QC16 of the discussion paper for a full definition of reliability and faithful representation). What is explicitly missing from the new definition is any mention of 'free from material error and bias', which was included in the previous definition of reliability and is now subsumed into verifiability and neutrality. If fair value is deemed better able to capture economic substance, then historic cost (despite its reliability) might be deemed an inappropriate measure. Similarly, a Fair Value View is accommodated by the absence of consideration of material error and bias, as fair value can rely more on estimation and subjectivity than alternative measurements.

As part of the discussion, the concepts of neutrality and prudence were considered. The present IASB Framework refers favourably to prudence and attempts to reconcile prudence with neutrality (similarly, ASB 1999, Statement of Principles) with the application of caution when making estimates so as not to overstate assets/income nor understate liabilities/expenses. This therefore helps the reliability of accounting information. The discussion paper explicitly rejects prudence because of its inconsistency with neutrality and freedom from bias. Therefore, there is now no need for a trade-off between neutrality and prudence. By rejecting prudence there are implications for stewardship. To ensure that financial performance is correctly reflected in financial reporting against any desire by managers to overstate income, for example, where managers are rewarded through shares or share options, there is a need for appropriate caution and reliability. Prudence helps address any agency tensions that may arise between management and present shareholders over reported financial performance. Furthermore, if prudence is removed and neutrality applied, current financial reporting standards would be inconsistent. This would mean a symmetric view of gains and losses. Currently IAS36 asserts that carrying values of assets can only be reduced by impairment testing. Similarly, IFRS4, dealing with insurance, states that the carrying value of liabilities can only be increased by liability adequacy tests. These both reflect prudence, rather than a symmetric neutrality, in valuing assets and liabilities respectively.

Phase B, the second proposed discussion paper, covering Elements and Recognition, was then considered. The focus of this work, which is still in progress, has been on the definitions of assets and liabilities, so reaffirming the balance sheet approach embedded in the current Framework. This emphasises the 'conceptual primacy' of assets and liabilities over income and expenses. The proposed definition of an asset deletes two significant phrases from the current IASB definition. First, that an asset arises 'as a result of past events' and secondly 'that future benefits are expected to flow from an asset'. These deletions were also applied to liabilities. The implications of these are that the deletion of a reference to past events reduces the importance of stewardship of past transactions and, in turn, may serve to impair the reliability of financial statements. Secondly, the deletion of expected future benefit is inconsistent with current recognition criteria (IASB Framework: 83), which explicitly recognise an element (asset) if it is probable that future economic benefit will flow to/from the entity. Any uncertainty would now be reflected in measurement rather than in recognition criteria. These two changes, both of which would accommodate a Fair Value View, potentially serve to erode the recognition criteria in the current Framework. Perhaps significantly, recognition criteria were not addressed as a part of Phase B.

Given the issues arising from assets and liabilities, the next element to be addressed in Phase B, equity, is perhaps even more problematic, particularly the distinction between equity and liabilities (on which FASB currently has a project). Equity is seen as a residual in the current Framework but this raises the issue of what constitutes equity as compared with liabilities, beyond issued share capital, especially given the current wide variety of financial instruments, such as options and warrants. One possible solution from the current FASB project is a 'claims approach' where all balance sheet credits are regarded as claims and there is no debt/equity distinction. An alternative approach is to classify two-tier equity, with the existing shareholders as one tier and then other equity instruments as the other tier. Such an approach would be consistent with the view whereby present shareholders are regarded as a special group, but would not fit in with IASB's broad-entity approach, as it would single out a specific group. Other elements such as income and expenses have yet to be discussed within Phase B, but given the balance sheet approach so far adopted it is likely that discussion of these will come as part of Phase E, Presentation and Disclosure. The IASB/FASB already have a joint project on performance reporting which favours a single comprehensive income statement. Comprehensive income includes changes in fair value measures but raises concerns over fair value volatility and reliability.

Phase D considers the Reporting Entity. One issue arising is in relation to holding company accounts, as opposed to group accounts. The current IASB entity-perspective view is that only one set of general purpose financial statements should be prepared, ie group accounts. For those who view present shareholders as a special group and see the need for a proprietary perspective, then holding company accounts, as well as group accounts, should also be prepared as they provide useful additional information to the current shareholders.

Phase C considers Measurement and while work has already started this will be a contentious area. One of the current Framework gaps has been clear guidance on measurement. This was avoided by earlier Frameworks, which reflected the indecisive outcome of the inflation accounting debate by discussing the desirable properties of measurement without advocating a single measurement objective. Broadly, this debate was about historical cost versus some version of current cost. More recently, as in IAS39 (Financial Instruments) and IAS41 (Agriculture), there has been an increased preference for fair value, defined as an exit (sale) value. The recent IASB discussion paper, based on SFAS157, defines fair value on an exit price, not a replacement cost basis, with transaction costs excluded. Exit price is based on transactions between market participants, thus being market based and non-entity specific. Clearly, based on current developments in accounting standards, fair value and its underlying assumptions have strong support. The debate has far wider concerns than just measurement, however, or the question of whether fair value is or is not a good measure. It concerns the purpose of financial accounting and the context in which it operates.

From the earlier discussions it is possible to identify two broad world views: the Fair Value View and the Alternative View. These are summarised with their respective implications below:

a) Fair Value View:
This is the view that is generally supported by FASB and IASB and is apparent in many of the proposed revisions of the Framework. The Fair Value View emphasises decision-usefulness as the sole objective of financial reporting and its relevance to current and prospective investors and creditors as the user groups. It emphasises the role of financial reporting in serving investors in capital markets To facilitate decision-usefulness, accounting information should reflect future, not past, transactions, and consequently forecasting and disclosing future cash flows is required to meet the principal need of those groups. Relevance is the primary characteristic required in financial statements, whereas reliability is less important and is replaced by representational faithfulness as an objective, implying greater concern for economic substance than for statistical accuracy. Current market prices, on an exit basis, give a neutral, non-entity specific informed view of cash flow potential. Markets are generally complete and efficient enough to provide evidence for representationally faithful measurement.

The implications of the Fair Value View are that present shareholders have no special status among investors, but form part of the wider investor community, and that stewardship is not a distinct objective of financial statements but, instead, market value is the universal concern. Accounting information (financial statements) will reflect future not past transactions and events, and such past transactions or events are only relevant as part of predicting the future. Thus cost (entry value) is an inappropriate measure as it relates to a past event whereas future cash flow will result from future exit measured by fair value. Prudence is a distortion of accounting measurement as it brings bias against neutrality and violates faithful representation. Overall, the measurement objective should be fair value, with the balance sheet as the most important statement, showing the current fair value of the entity, supported by a comprehensive income statement.

b) Alternative View:
The Alternative View presented brings together the collection of issues raised by a range of observers typically commenting on particular issues rather than developing a coherent framework model. This does not prevent the formulation of an Alternative View; rather, it shows its origins and recognises the variety of potential issues that exist. The main features of this Alternative View are that present shareholders of the holding company do have a special status. They are the owners of the business and need to be informed of past transactions and events as well as future cash flows, so that stewardship is a distinct objective of financial reporting and ranks equally with decision-usefulness. Past transactions and events need to be reported as they are important for both stewardship and as inputs for predicting future cash flows. Future cash flows may be endogenous, and financial reporting relieves asymmetry in an uncertain world with incomplete and imperfect markets, in which opportunities are entity

specific, so reliability within financial statements does matter and is an essential characteristic.

The following implications arise from the Alternative View. The information needs of present shareholders, including stewardship requirements, must be met. Past transactions and events are relevant information and, together with other recognition criteria, enhance reliability. Reliability of financial statements can be further enhanced by prudence. Cost is a potentially relevant measure as an input to the prediction of future cash flows as well as for stewardship purposes. The economic environment is characterised by imperfect and incomplete markets in which opportunities are entity specific and so entity-specific assumptions reflecting real opportunities available are relevant and financial statements should reflect such an entity-specific position.

The underpinning market assumption of the Alternative View that markets are imperfect and incomplete does not lack theoretical support. It is compatible with Hicks (1946) and with Edwards and Bell (1961), whose analysis emphasises income rather than the balance sheet and considered how ex post accounting income, based on past transactions and events, could be used to evaluate performance. This is based upon current cost measures, not fair value. Beaver and Demski (1979) argued that markets are imperfect and incomplete and that accounting provides useful information rather than definitive measures.

The IASB view has usually been consistent with a Fair Value View. Nonetheless, a number of IASB proposals have been criticised, in some cases showing alternative views from within the board. Some IASB proposals affected by the Alternative View are discussed below.

Present shareholder focus

IFRS2 share-based payment measurement should be based on exercise date, not grant date from the perspective of present shareholders.

Entity-specific assumptions

IAS36, Impairment of Assets, bases recoverable amounts on projected cash flows, which will inevitably be based upon entity-specific management forecasts. IAS37, Provisions, similarly allows entity-specific assumptions of the best estimate to settle an obligation at the balance sheet date.

The relevance of cost

The use of historic cost measures for recognition of assets and liabilities is widespread in current IASB and ASB standards. SFAS157 proposals preclude the interpretation of fair value as replacement cost. This would change practice in terms of IAS16, Property, Plant and Equipment, and IAS17, Leases, where replacement cost may seem a more relevant measure of future cash flows. The use of fair value in IAS39, Financial Instruments, can give rise to 'day one' profits, although such profits are not yet earned. This is why retailers, for instance, conventionally record stock at cost not selling price.

Reliability and Prudence

In IFRS 3, purchased goodwill is measured at cost rather than at fair value. Amortisation of goodwill was replaced by impairment testing, which should be prudent although it does not include a subsequent cash-flow test of impairment value. Impairment is asymmetric and not neutral in its application to purchased goodwill.

Recognition criteria

The two recognition criteria in the existing IASB Framework are the probability that the entity will receive future cash flows from an asset, deleted in the proposed asset definition, and reliability of measurement, now replaced in the new proposals by faithful representation.

Overall, the Fair Value View emphasises the role of financial reporting in serving investors in capital markets, which are viewed as complete and competitive. Financial statements reflect forward-looking content, impounding future cash flows from a non-entityspecific market perspective. The Alternative View also seeks to serve investors, broadly defined, but gives special accord to present shareholders and equates stewardship as an important and distinct function of financial reporting. This approach assumes information asymmetry and that imperfect and incomplete markets are common. Past transactions and events are important for accountability as well as being relevant in predicting future cash flows. Given the competing demands of reliability and relevance, there exist a multitude of measurement *bases* that can be applied in current financial statements, negating the adoption of a universal single measurement. There is, however, a need for a single measurement objective.

2.5 COMMUNICATION BETWEEN MANAGEMENT AND STAKEHOLDERS: A CASE STUDY. BILL MCINNES, VIVIEN BEATTIE, AND JACKY PIERPOINT

Bill McInnes and Vivien Beattie presented their recent research examining communications between company management and stakeholders. The research was funded by the ICAEW Centre for Business Performance and a briefing or full research report is available through the ICAEW (www.icaew.com/index.cfm?route=153386). The presentation covered the key aspects of their research into stakeholder communications from empirical findings through to theorising on stakeholder communication uptake. The research was based upon a single case company and involved internal interviews with key company managers and directors, and stakeholder interviews with internal stakeholders (employees) and a comprehensive range of external stakeholders.

A common focus of previous accounting research into communication between management and stakeholders has been the annual report. There has been very little investigation of other information sources used by stakeholders. Previous research has also tended to focus on a relatively small number of stakeholder groups, primarily equity investors and analysts, and consequently does not address the information usage by other groups. New reporting models have been proposed calling for the annual report to be redesigned to fulfil more of the needs of a range of stakeholder groups (see ICAEW 2003 for a summary and discussion).

The research by McInnes et al. represents a major contribution to the literature on communication between management and stakeholders. It adopts a multi-stakeholder group perspective to examine a wide range of the information sources and communication channels used by the case company and by third parties (for instance, analyst reports or news media coverage) in their stakeholder communication. The broad research aims were:

- to identify the range of information sources and communication channels used by a case company and third parties to communicate with the company's stakeholders
- to examine the extent to which the information sources were used and the communication channels were accessed by a range of stakeholder groups.

For the research, a single case company was selected and full access was obtained to relevant management and internal and external stakeholders. In total, five key company management interviews were performed and 36 stakeholder interviews were conducted during the research phase covering the following stakeholder groups:

- equity investors
- equity analysts
- credit investors
- credit analysts
- credit raters
- private shareholders
- employees
- suppliers
- customers.

The case company is a UK- and US-listed regulated utility and accordingly has a wide reporting remit and a wide range of stakeholder groups, which made the company appropriate for the empirical research.

Key findings of the research covered the following aspects:

- conceptual issues
- communication offerings
- stakeholder communication uptake and emergent theoretical model
- other miscellaneous observations.

Each of these main areas is summarised in turn below.

i. Conceptual issues

Recent conceptual framework documents (eg IASB 2006) have recommended that financial reporting should provide information from which it is possible to assess a company's future cash flows. This objective is particularly relevant to stakeholders who are finance professionals. Major companies already generate such information internally to enable them to forecast future earnings, free cash flow, etc, but the issue remains as to the extent of the external disclosure of such information. At present, limited disclosure does exist. The case company did provide such forecast disclosure to its credit rating agencies. While such information may be (share) price sensitive, companies are permitted by the Listing Rules (FSA 2007) to provide such information on a confidential basis to credit rating agencies. The raters perceive the forecasts as important in the rating process. Given the confidential nature of the disclosure and the surrounding Listing Rules regulatory framework, widespread disclosure would be problematic, and hence leaves the current position where credit rating agencies have greater access to some information than do other stakeholder groups. This opens the question for the IASB of whether, and if so how, a similar approach for forecast disclosures could be adopted for other stakeholder groups.

Wider information sources are then considered, and a clear distinction made between information sources and communication channels. This distinction is not made in the extant literature. Information sources are the content (eg annual report) whereas communication channels are the medium of dissemination (eg paper copy or website). For effective stakeholder communication both possible sources and appropriate channels need to be considered by companies. A wide array of information sources are included in the research, which covers, inter alia:

- company announcements
- annual reports
- social and environmental reports
- question and answer sessions, and
- forecasts.

Similarly, a wide range of communication channels exist to disseminate information and include, for instance:

- newswires
- newspapers
- website
- results meetings
- CDs
- employee roadshows
- one-to-one meetings
- intranet
- email.

Depending on the information source, an appropriate means of communication can be adopted to optimise take-up by stakeholder groups. Interestingly, all stakeholder groups, especially the finance professionals, viewed the website as an electronic library of background information rather than as an interactive forum.

The appropriate communication channel may also be dictated by the timeliness required for the information. Often, the arguments about timeliness relate to finance professionals, for whom it is important that information is disseminated as soon as it becomes available (eg through announcements or presentations). Paper-based dissemination results in a time lag and so is less useful for finance professionals. Nonetheless, it is still useful for more passive stakeholder groups, so that the annual report, as a paper document, can be used by employees, customers or suppliers to assess company performance. Thus information to the latter groups is timely if it is able to inform and influence current and future decisions.

ii. Communication offerings

Information sources available to stakeholders are provided by the case company and by third parties. From the case company, some of the sources such as the annual report and press releases are directed at a general audience of all stakeholders. Other sources of company information are targeted at specific stakeholder groups, for instance the forecasts for credit raters, and in those instances such information is not available to other stakeholder groups. Similarly, some communication channels are available only to specific groups, such as the road-shows for employees. In addition to company sources, stakeholders are also able to access third-party information including equity analysts' reports, news and media coverage and regulatory reports. All stakeholder groups made use of such third-party sources for three main reasons: to obtain new information; to obtain benchmarking information; and to access expert analysis.

Given the targeted dissemination of some of the information sources, stakeholder groups have access to a differentiated range of information. Some stakeholders are more privileged than others in the information available to them and in the communication channels to which they have access. Credit raters receive forecast information from the company and major equity investors benefit from one-to-one meetings with a company's senior management. Similarly, third-party conferences are available to finance professionals but not to private shareholders. Thus the stakeholder information field is not level, but distorted in favour of some more privileged stakeholder groups.

iii. Stakeholder communication uptake and emergent theoretical model

Differences were found among the stakeholder groups in the level of information uptake and this was broadly a function of the importance of the case company to the stakeholder group. Two meta-stakeholder groups were identified, namely finance professionals (equity and credit investors, sell side equity and credit analysts, and credit raters) and the groups that were not finance professionals (private shareholders, employees, suppliers and customers). The finance professional group used (accessed) a wider range of information sources (communication channels) more intensely (frequently) compared with the groups that were not finance professionals. Within the finance professional group, the sell side equity and credit analyst groups used (accessed) a wider range of information sources (communication channels) than the equity and credit investor groups. This may be because the latter group has to manage a more diverse and larger range of investments and thus needs to focus on key information sources while lacking the time to adopt a wider search of information sources. Furthermore, the equity and credit investors rely upon their respective analysts for summaries of the wider information through their analyst reports and recommendations.

While there was some homogeneity within the groups of finance professionals for comparison of uptake, there was less homogeneity within the groups of stakeholders who were not finance professionals, particularly the supplier group. This may have arisen from the suppliers' different and varied relationships with the case company. The differences between the meta-groups were also highlighted by their use of the separate social and environmental report. This was not used by the finance professional groups, consistent with prior research, but was used by employees and suppliers.

Based upon the empirical findings a generic grounded theory model of stakeholder communication uptake was proposed: that the overall level of uptake is influenced by the importance of the company to the relevant stakeholder group. Communication uptake fulfils four distinct roles and reflects the need for:

- acquisition of timely, decision relevant information
- availability of reference source to facilitate company monitoring
- a means of assessing the level of trust that can be placed in company management, and
- a means of engaging with other stakeholders to seek their views on the company.

iv. Miscellaneous observations

The annual report, while important to some stakeholders, is not the only information source used by them, even though much accounting research has traditionally focused and relied upon the annual report as a prime reporting document. Key roles were identified in relation to stakeholder use of the annual report. For the finance professional groups, although it is not a timely document for capital market decisions, it is used as a historical reference document. For groups other than finance professionals, the annual report contains the first formal company results information and associated narrative and can be used as part of current and future decision making about the company. Further, the narrative sections, particularly the Chairman's statement and CEO report, are used by private shareholders as a means of assessing the trustworthiness of senior management, whereas such narrative sections were not seen as new information by the finance professional groups, who regarded the 'front end' as propaganda material.

In general, company management target the preliminary results narrative at the finance professional groups whereas the annual report narrative is aimed at a more general audience. Thus, in any future review of the regulation of narrative reporting and its influence over decision making, both preliminary results and annual reporting narratives should be addressed. Finally, some of the finance professionals preferred the more regulatory-driven US narrative reporting to the more voluntary UK reporting framework. This suggests that such narrative results in higher-quality disclosure compared with the more voluntary-based UK narrative reporting disclosures.

Overall, the research highlights the range of both information sources and communication channels available from companies (and third parties). It provides evidence of the extent to which each information source is used and each communication channel is accessed by each of nine stakeholder groups. A generic grounded-theory model of stakeholder uptake is developed that identifies four distinct roles in which stakeholders used the information. The findings make a number of useful contributions to the literature and should provide the basis for future research in the area.

3. Discussion

In sum, therefore, these five papers provide a critical new look at some perennial accounting problems. Bromwich, Macve and Sunder's paper critically examines the FASB/IASB Conceptual Framework Project; its assertion of the primacy of assets approach as the bedrock of the framework and its claimed underpinning by Hicks. Additionally, it questions the Boards' pitting of 'conventions' against 'conceptual principles'. The primacy of assets approach supports the proposition that the concept of income is founded ultimately on the definition of assets and that income is the increase in net resources in terms of changes in assets and liabilities over a time period, and thus is objectively determined. It is claimed that such primacy is derived from Hicks' definition of income (1946). The authors argue that Hicks has been misquoted and not considered in full, with his results taken out of context and thus misapplied in their use, and hence this undermines the primacy of assets approach. The paper addresses the key differences between the IASB/FASB approach and that of Hicks as regards their respective views of income, and covers in turn the issues of net assets vs. firms, objective vs. subjective measurement, income ex post vs. income ex ante, and finally, Income No.1 vs. Income No. 2. As more companies are now reporting levels of permanent or maintainable income (core EPS), the paper contends that given such disclosure, assets and liabilities can be derived from income rather than vice versa and consequently the primacy of assets approach is dismissed.

Chisman gave insights from a practitioner perspective (and drew on his involvement with accounting standards as a former member of the Financial Reporting Council) on the suitability and appropriateness of the competing bases of accounting measurement in relation to satisfying the user requirements and purposes of financial statements. The paper outlined the current measurement bases: recoverable historic cost (RHC), fair value (FV), value in use (ViU) and the mixed basis that is currently used within financial statements. Chisman considered the relationship of ownership to the needs of the users of financial statements and the differences between private and public companies. If this difference is understood then appropriate bases of measurement for the preparation of financial statements can be advocated that satisfy the distinct user needs. For private companies, where shareholders are themselves directors of the business, the fundamental purpose of financial statements is creditor protection. In this instance, RHC would be adopted as providing a simple and objective basis of measurement. For public companies and larger private companies, there is a dual purpose: creditor protection and investor protection (ie, value creation and assessment of management performance requiring cash-flow forecasts). On the basis of measurement, there is trade-off between the objective, historic information of RHC compared with the subjective, forecast information of ViU. To satisfy the dual needs of creditor and investor protection a dual measurement basis would be adopted. The accounts of public companies would not only report all items under RHC, but would also report forecast and value-driven information under ViU. Creditor protection is covered by RHC and the dialogue between managers and investors under ViU focuses on value creation and performance evaluation.

Martin set out his arguments for a single basis of measurement to reduce the current accounting complexity borne from multiple bases. The focus of the paper is on the adoption of fair value accounting as an appropriate measurement basis. This allows a focus on decision-usefulness, provides an objective, market-specific (rather than entity-specific) measurement base to capture consistent market values of items at any one moment so as to facilitate greater business comparability. Fair value recognises the change in asset value over time and its consequent impact on profit, and compared with RHC is not beset by transactional differences related to the historic purchase price of assets. The paper cited examples of where fair value is already applied (see for instance IAS39-41), but considered how it could be universally applied to all items rather than just specific items covered by current standards. SFAS157 provides three hierarchical levels of fair value application, reflecting market and data conditions that could be drawn upon to apply fair value to the individual components of the financial statements. The issue of the trade-off between reliability and relevance is addressed in the paper. While fair value provides relevant decision-useful information it also results in recording and accounting for asset price volatility and by moving away from a transactions base there is early recognition of gains that may not be reliable or materialised. Issues of reliability are now evident in the light of Enron and, since Martin's presentation, in the current subprime crisis. A single measurement base could reduce accounting complexity, but may require in its achievement wholesale revision of the conceptual framework.

Whittington's paper addresses the conceptual framework debate and its implications for the basis of measurement and is part of a wider debate on the purpose of financial accounting and the context in which it operates. He presented two world views: A Fair Value world view implicitly favoured by IASB, with decision-usefulness as the primary focus of financial reporting and an Alternative View (compatible with Hicks, 1946, and Edwards and Bell, 1961) which recognises stewardship as well as decision-usefulness as dual objectives of financial reporting. The Fair Value View is based on the assumption that markets are relatively perfect and that financial reporting needs to address the needs of passive investors and creditors. Fair value emphasises decision-usefulness, focuses on forecasting future cash flows, not past transactions, with relevance rather than reliability being the primary characteristic of financial statements. The Alternative View presented recognises that markets are relatively imperfect and so the reliability of financial statements matters and that the needs of current shareholders and the importance of stewardship ranks equally with decision-usefulness. Throughout the paper the relevance and reliability debate of financial reporting is addressed, linking into consideration of, inter alia, prudence, the conceptual primacy of assets and the meaning/definition of equity.

The paper provides a review of the IASB/FASB Joint Conceptual Framework Project and sets out in detail a critical review of the first Discussion Paper, 'Objectives of Financial Reporting and Qualitative Characteristics of Decision-useful Financial Reporting' before addressing subsequent discussion papers. The paper concludes with a summary of the two world views and their implications and reviews current IASB proposals showing how they are affected by the Alternative View.

The final paper in the series by McInnes, Beattie and Pierpoint provided an empirically-based examination of communications between a single case company's management and a range of stakeholders: investor and analyst groups, credit raters, employees, suppliers and customers. The paper addressed in turn conceptual issues, communication offerings, stakeholder communication uptake and various miscellaneous topics. The researchers developed a grounded theoretical model of stakeholder communication, which proposes that the overall level of communication uptake is influenced by the importance of the company to the relevant stakeholder group and that communication uptake fulfils four distinct roles. Important issues are raised, such as the consideration of publication and release of forecast information to all stakeholders and the current differentiated stakeholder access to various sources of information. The role and usage of the annual report and its contents to stakeholder groups was considered. From the empirical data, and the levels of access to information, two meta stakeholder groups were identified, finance professional groups and groups that were not finance professionals.

The papers in Table 1 have been organised into two groupings rather than in their actual order of presentation. In the first group (Bromwich, Macve and Sunder; Chisman; Martin; and Whittington) four very different reflections on measurement are presented. The fifth paper by McInnes, Beattie and Pierpoint is listed separately as it is primarily concerned with financial communication and stakeholders rather than measurement.

All the authors, except for Sunder (from the US) are British, but have very different perspectives on their topics. Three papers emanate from the academic sector. Bromwich and Macve are professors at the London School of Economics, their co-author, Sunder is a professor at Yale; Whittington is a professor at Cambridge University; and McInnes and Beattie are professors at the Universities of Stirling and Glasgow, respectively. By contrast, Chisman is an accounting practitioner and former finance director of Stakis plc and Thorn Ltd and also former member of the Financial Reporting Council and finally Martin is head of financial reporting at ACCA. The authors, therefore, bring a variety of different approaches to their papers.

These differing backgrounds were reflected in the nature of their outputs. Chisman and Martin both presented their views to inform the policy discussion and have a practitioner and professional accounting perspective. The remaining three papers are more academic in orientation. Bromwich, Macve and Sunder's paper is available as a working paper on the LSE website (the full web reference is given within the paper commentary). McInnes, Beattie and Pierpoint's paper is available both as an ICAEW report and also a briefing document (again the full reference is given within the paper commentary) and Whittington's paper is published in an Australian academic journal, *Abacus*, 44/2, 2008.

The four papers that look at measurement show great variety in terms of focus, research approach and source materials. The Bromwich, Macve and Sunder paper examines a fundamental premise that has underpinned modern thinking about accounting. It revisits an old accounting chestnut: the debate on whether measurement should start with income (and the income statement) and thus have the assets and liabilities (broadly, the balance sheet) as residuals or conversely whether it should begin with assets and liabilities measurement and treat the income statement as residual. The latter is the approach used in the IASB's conceptual framework. Bromwich, Macve and Sunder critically evaluate the assumptions that underpin this approach. By contrast, Chisman focuses on a different problem: the interesting question of which of four commonly used bases of accounting measurement (ie, recoverable historic cost (RHC), fair value, value in use and the mixed basis) could be used for public and private companies. Martin's main focus is on fair value. He considers its growing use, the variety of ways in which it might be used, and its weaknesses and criticisms. In addition, Martin calls for a revision of the conceptual framework. Finally, Whittington, in a carefully argued approach, outlines two political world views underlying the current framework and measurement debate: a 'Fair Value View' implicitly preferred by the IASB and an Alternative View. Whittington, therefore, produces an alternative construct for financial reporting measurement. Meanwhile, Bromwich, Macve and Sunder suggest a different starting point and Chisman suggests a differential approach to measurement.

Table 1: Thematic overview of the five papers presented

Authors	Background	Output	Focus	Research	Source materials	Key fndings
Bromwich, Macve and Sunder	Academic: Macve is academic adviser to the ICAEW's Centre for Business Performance. Bromwich is a former member of the ASC	Academic working paper	Income measurement and conceptual framework	Critical examination of prior literature with normative reasoning	Hicksian views of income and conceptual framework	Companies often report levels of permanent income and this can be used as the basis for determining useful reporting to complement reporting of changes in assets and liabilities
Chisman	Practitioner: former FD of Stakis plc and Thorn Ltd, and former member of the Financial Reporting Council	Presentation	Basis of measurement	Critical examination of practice using professional experience	Current standards	A dual reporting measurement scheme in which private companies use recoverable historic cost. A dual basis for public companies: recoverable historic cost and value in use
Martin	Professional: accountancy body, head of financial reporting, ACCA	Presentation	Fair value	Critical review of current literature	Current IASB and US standards and conceptual theory	An abundance of measurement bases and differing treatment of items within financial statements. Growth in fair value. Conceptual theory revision may be necessary
Whittington	Academic: with standard-setting experience and member of the Accounting Standards Board and formerly International Accounting Standards Board	Academic paper in Abacus (2008)	Fair value and conceptual framework	Critical review of current thinking using experience as a policy setter	Current IASB and US standards and conceptual theory	Outlines an Alternative View to the current Fair Value View that gives special accord to present shareholders and equates stewardship as a distinct and equal function to decision-usefulness in financial reporting
McInnes, Beattie and Pierpoint	Academic	ICAEW Research Report (2007)	Communication between management and stakeholders	Empirical study using interviews	41 semi-structured interviews with 5 key company officers and 36 stakeholders from 9 stakeholder groups	Companies communicate with stakeholders via a range of information sources and communication channels. Some stakeholder groups in a more privileged position than others. Development of a generic model of stakeholder communication uptake

There is less difference between the four *research approaches* to measurement. All four authors, in their own way, critically review the current standards and conceptual theory, but from very different backgrounds. Bromwich, Macve and Sunder, and Whittington start from academic backgrounds. In Bromwich and Macve's cases that is mediated by their roles as a former member of ASC and as academic adviser to the ICAEW's Centre for Business Performance respectively, whereas in Whittington's case his academic standpoint is informed by his experience and knowledge as a standard setter for both the Accounting Standards Board and International Accounting Standards Board. Chisman approaches the topic of measurement from his professional and also policy-relevant experience as a FTSE250 finance director and former member of the Financial Reporting Council (and also ICAEW Financial Reporting Committee), while Martin critically reflects on fair value in his role as the head of financial reporting at the ACCA. This enables rich debate around the subject areas and highlights the current complexities from both a conceptual and theoretical perspective. A further challenge is the practical orientation of any future conceptual framework and basis of measurement. Debates such as these are, therefore, vital to reflect the inputs from academic, professional and practitioner viewpoints.

Whereas Chisman and Martin draw primarily on their personal experience and a critical evaluation of the current standards and the conceptual theory, Bromwich, Macve and Sunder, and Whittington also draw on accounting theorists. In the former case, Bromwich, Macve and Sunder draw on the famous works of Hicks (1946, 1948 and 1979, as well as Paish, 1940) to support their argument that the IASB has used Hicks out of context to support the objectivity of the primacy of assets. Whittington also draws upon Hicks (1946), and Edwards and Bell (1961) for theoretical support for his underpinning assumption for the Alternative View that markets are imperfect and incomplete. The use of Hicks to support IASB/FASB fair value arguments is critically questioned by both Whittington, and Bromwich, Macve and Sunder.

The McInnes, Beattie and Pierpoint paper addresses a different issue from the other four. It is concerned with communication between management and stakeholders. This looks back to the debate in the UK, for example, on *The Corporate Report* in 1975, which was published to create a focus on the usefulness of published financial statements. The authors' research approach was an empirical study using 41 interviews. These interviews were then used to document a range of information sources and communication channels as well as to develop a generic grounded theory model of stakeholder uptake.

4. Conclusions

The papers presented in this report provide new insights into perennial accounting problems, particularly those of measurement, fair value, conceptual theory and stakeholder communication. Bromwich, Macve and Sunder argue that income can be used directly as a complimentary basis to reporting assets and liabilities rather than being derived from them. Chisman advocates a dual measurement system for private companies and public companies. Martin points out that the growth in fair value may require a revision to the conceptual framework. Whittington outlines an alternative world view underpinning the current measurement and conceptual framework debate based on special recognition of present shareholders and incorporating stewardship. Finally, McInnes, Beattie and Pierpoint construct a generic grounded theory model of stakeholder uptake of various information sources and communication channels.

All five papers present fresh insights into current financial reporting while addressing issues that have troubled both accounting academics and practitioners over many generations. What is particularly enriching is the differences in background, focus, research approach and source materials. The authors are academic, practitioner or professional in orientation and the consequent debate draws upon this experience and provides a richness of discussion, combining research, practice and policy. The focus varies between fair value, the basis of financial reporting measurement, income measurement in relation to conceptual theory, and communication between management and stakeholders. Four of the papers draw their inspiration from a critical review of current thinking, while the McInnes, Beattie and Pierpoint paper is based on an interview study. In terms of source materials, four of the authors are primarily interested in the current standards and conceptual theory, with two sets of authors (Bromwich, Macve and Sunder, and Whittington) drawing upon accounting theorists such as Hicks, and Edwards and Bell.

Given these differences in background, focus, research materials and source materials it is unsurprising that the authors produce very different key findings, which we summarise below.

- Permanent income can be used as the basis for determining useful financial reporting to compliment changes in assets and liabilities (ie not simply using changes in assets and liabilities to determine income as per the IASB conceptual framework) (Bromwich, Macve and Sunder).

- Hicks' definition of income (1946) has been misquoted and misapplied to support the primacy of assets approach (Bromwich, Macve and Sunder).

- A dual measurement system is possible in which private companies use recoverable historic cost and public companies use both recoverable historic cost and value in use, with the consequent dismissal of fair value as a useful basis of measurement (Chisman).

- Dual reporting would satisfy the needs of creditors (RHC) and investors (ViU). Dual reporting would be undertaken by all public companies and any private companies that elected for dual reporting beyond RHC (Chisman).

- There are a variety of different measurement bases currently used in financial accounting. The use of fair value is growing, but it has limitations and weaknesses. A revised conceptual theory may be necessary (Martin).

- Fair value can be used as a single measurement basis to reduce accounting complexity but the issue of trade-off between relevance and reliability and need for relevance within financial statements still needs resolving (Martin).

- Two potential world views are possible. First, the Fair Value View, implicitly preferred as the basis of measurement by the IASB, based on a relatively perfect market, emphasising decision-usefulness and relevance to current and prospective investors and creditors, with a focus on forecasting future cash flows and being based on market sale price, ignoring transaction costs and free of entity-specific assumptions. Second, an Alternative View based on imperfect markets, meeting the needs of current stakeholders and explicitly recognising the dual importance of stewardship alongside decision-usefulness (Whittington).

- Companies use a range of information sources and communication channels to communicate with stakeholders. Two meta-stakeholder groups: finance professional groups and groups that are not finance professionals are identified. The overall level of uptake, it is proposed, is influenced by the importance of the company to the relevant stakeholder group. Communication uptake reflects the four roles (timely, decision-relevant information; reference source; level of trust in company management; and means of engagement with other stakeholders) (McInnes, Beattie and Pierpoint).

- Different stakeholder groups have differential access to information sources and channels of communication. There should be consideration of a wider release of forecast information to stakeholder groups (McInnes, Beattie and Pierpoint).

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Appendix 1

Declarations of Co-Authorship of Published Work

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DECLARATION OF CO-AUTHORSHIP OF PUBLISHED WORK

(Please use one form per co-author per publication)

Section A
Name of candidate: Richard Slack

Name of co-author: Dr David Campbell

Full bibliographical details of the publication (including authors):

Campbell, D. and R. Slack (2006), 'Public visibility as a determinant of the rate of corporate charitable donations', *Business Ethics; A European Review*
January 2006, Volume 15, Number 1, pp17-26

Section B
DECLARATION BY CANDIDATE (delete as appropriate)

I declare that my contribution to the above publication was as:

(ii) joint author

Signed: ....(candidate) 16/7/09............(date)

Section C
STATEMENT BY CO-AUTHOR (delete as appropriate)

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or (ii) ~~**I do not agree with the above declaration by the candidate for the following reason(s):**~~

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DECLARATION OF CO-AUTHORSHIP OF PUBLISHED WORK

(Please use one form per co-author per publication)

Section A
Name of candidate: Richard Slack

Name of co-author: Professor Geoff Moore

Full bibliographical details of the publication (including authors):

Moore, G., Gibbon, J. and R. Slack, (2006) 'The mainstreaming of Fair Trade: a critical marketing perspective', *Journal of Strategic Marketing,*
December 2006, Volume 14, Number 4, pp329-352

Section B
DECLARATION BY CANDIDATE (delete as appropriate)

I declare that my contribution to the above publication was as:

(iii) minor contributing author

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or **(ii) ~~I do not agree with the above declaration by the candidate for the following reason(s):~~**

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DECLARATION OF CO-AUTHORSHIP OF PUBLISHED WORK

(Please use one form per co-author per publication)

Section A

Name of candidate: Richard Slack

Name of co-author: Jane Gibbon

Full bibliographical details of the publication (including authors):

Moore, G., Gibbon, J. and R. Slack, (2006) 'The mainstreaming of Fair Trade: a critical marketing perspective', *Journal of Strategic Marketing*, December 2006, Volume 14, Number 4, pp329-352

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August 2007, Volume 74, Issue 2, pp191-200.

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DECLARATION BY CANDIDATE (delete as appropriate)

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Section A

Name of candidate: Richard Slack

Name of co-author: Philip Shrives

Full bibliographical details of the publication (including authors):

Slack, R. and P. Shrives, (2008), 'Restoring legitimacy and social reporting by Premier League football clubs; the first ten years', *Journal of Applied Accounting Research* June 2008, Volume 9, Number 1, pp17-28.

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(ii) joint author

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Name of co-author: Professor Geoff Moore

Full bibliographical details of the publication (including authors):

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Campbell, D. and R. Slack (2008), *Social and Environmental Narrative Reporting; Analysts' Perceptions*, Association of Certified Chartered Accountants (ACCA)
Research Summary Report
Principal author to note for inclusion

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Section A
Name of candidate: Richard Slack

Name of co-author: Professor Mike Jones

Full bibliographical details of the publication (including authors):

Slack, R. and M. Jones, (2009), *The Future of Financial Reporting 2008: Measurement and Stakeholders*, Association of Certified Chartered Accountants (ACCA) Published Discussion Paper

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Appendix 2

Campbell, D., McPhail, K. and Slack, R. (2009), 'Face work in annual reports: a study of the management of encounter through annual reports, informed by Levinas and Bauman', *Accounting, Auditing & Accountability Journal*, 22 (6), pp. 907-932.

The current issue and full text archive of this journal is available at
www.emeraldinsight.com/0951-3574.htm

Face work in annual reports

A study of the management of encounter through annual reports, informed by Levinas and Bauman

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Abstract

Purpose – Annual reporting has moved from the conveyance of "simple" accounting numbers and more towards narrative, graphical, pictorial and broader aesthetic content conveyance. At the same time, there has been a small but growing discussion of the work of Emmanuel Levinas and Zygmunt Bauman and in particular the ethic of the Other. The aim of this paper is to explore the presence of faces in annual reports.

Design/methodology/approach – Based on initial observations from the analysis of human representations in the annual reports of 14 companies for all years 1989 to 2003 (210 annual reports), the paper interprets the increase from a Levinasian perspective, drawing substantially from Bauman's articulation of Levinas' ethic of the Other. Particularly within the work of Levinas, this ethic is articulated through the nakedness of the face. Analysis is partly performed through illustration of the site of audiencing, a key visual methodology, in annual report images.

Findings – A significant rise in total human representation over time is interpreted in Levinasian terms and the range of sites of audiencing is demonstrated. Arguments are discussed that suggest a counter-hegemonic understanding of the corporations' responsibility to the Other.

Originality/value – The paper provides a critical analysis of what this kind of face work means within the context of Levinas' ethics of the Other. The paper explores what this kind of face work means for the possibility of Levinasian-inspired moral development and the potential for a counter-hegemonic face work that may promote accountability.

Keywords Annual reports, Accountancy, Visual media

Paper type Research paper

This paper was presented at the Interdisciplinary Perspectives on Accounting Conference at Cardiff in July 2006 and at the CSEAR summer school in September 2007, at both of which the authors received many helpful pointers including sage advice from Michael Jones and Jesse Dillard. The two anonymous reviewers for *AAAJ* were very helpful in developing the paper and the authors would also like to thank the Guest Editors of the special issue in which this paper appears for their encouragement and support throughout the whole process.

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It is only in a world without a face that absolute nihilism can establish its law (Finkielkraut, 1997, p. 113).

1. Introduction

The aim of this paper is to explore the presence of faces in annual reports (Plate 1). We introduce a number of observations on the changing portrayal of human faces in annual reports then, drawing on the work of Emmanuel Levinas and Zygmunt Bauman, explore two general and related questions. First, to what extent do corporations use images of human faces in their annual reports, and second, how do these images "work"?

There has been a perceptible change in company annual reports over the past few decades. They now look and quite literally feel different. Campbell *et al.* (2006) noted a substantial lengthening of the documents over time from an average of 37 pages in 1974 to 90 pages in 2000. In addition, however, Hopwood (1996, p. 55) observed that, "the accounting data are now a mere technical appendix to a highly sophisticated product of the design environment". Annual reports no longer just communicate simple financial data: they are designed to convey complex multi-messages to a number of different constituencies and are now "used" by executives, sales representatives and personnel departments for a number of different purposes (Preston *et al.*, 1996). As a consequence, academic attention has moved away from the numbers to the narrative (Smith and Taffler, 2000), graphical (Beattie and Jones, 2002), pictorial (Davison, 2004, 2007) and broader aesthetic content of reports (Preston *et al.*, 1996). At the same time, within a completely different stream of the accounting ethics literature, a discussion has emerged concerning the work of Emmanuel Levinas and in particular his ethic of the Other (Shearer, 2002; MacIntosh, 2004; Roberts, 2003; McKernan and Kosmala MacLullich, 2004): an ethic that is articulated by Levinas,

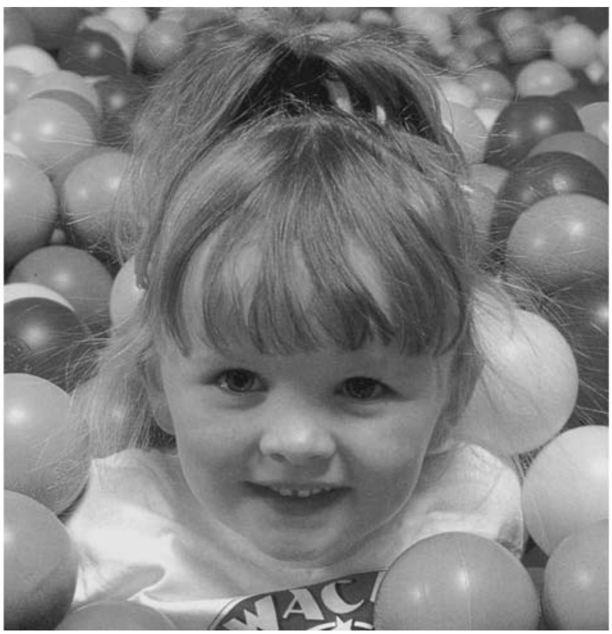

Plate 1.

more than analogically through the naked face. Bauman's sociological translation of Levinas has also appeared in the literature specifically in relation to the Holocaust (see for example, McPhail, 2001; Funnell, 1998). This paper brings both streams of literature together through an analysis of human faces in annual reports.

Commencing from an analysis of the annual reports of 14 UK FTSE top 100 companies, each over a 14-year period, the paper notes firstly that there has been a significant increase in human representation, in the form of the human face, in annual reports. This observation provides the basis for a general reflection on what this may mean when viewed through Levinas's and Bauman's work. In particular, we draw on some critical visual studies to explore the kinds of work that faces do on observers and we then discuss what this work means for the possibility of a Levinasian confrontation with the face of the Other. As such the paper represents a response to Preston et al's. (1996, p. 113) call over a decade ago for an increased, "critical dialogue that focuses upon the representational, ideological and constitutive role of images in annual reports".

The remainder of the paper is structured as follows: the next section outlines the theoretical foundation for the study. We provide a brief discussion of the changing nature of corporate annual reports; briefly delineate Levinas' ethical phenomenology and explain how Zygmunt Bauman translates Levinas into a form of sociological analysis. Section 3 focuses on our first question and briefly describes the results of a small empirical study of the emergence of human faces in corporate annual reports. Section 4 focuses on how these faces might be seen to work. The section draws on some critical visual studies literature in order to explore the nature of the work accomplished by pictures of faces in positioning of spectators. We then proceed to engage with the final step in our analysis: the anchoring of these images within the annual reports in particular. The paper concludes in section 5 with a summary of our main contentions.

2. Literature and context

Design and the annual report

The annual report has become the focus of increased attention over recent years. There are seemingly now a broad range of factors impinging upon and influencing the composition and look of these reports (Hopwood, 1996). It is now a complicated admixture of voluntary and non-voluntary disclosure (Stanton and Stanton, 2002) and there is a growing awareness of the multifaceted and complex role it plays in communicating information to the corporation's target audience(s). The corporate annual report has thus metamorphosed into a marketing and public relations document that reflects both the organisation's consciousness of its audience (McKinstry, 1996) and its self image (Roberts, 2003). The composition of the report, the narrative, images, graphs and numbers, are marshalled to convey a particular message to the firm's stakeholders, and primarily its financial stakeholders, although its influence and impact extends far beyond this group (McKinstry, 1996).

Different studies have focused on various emergent characteristics of this new form of annual report. Smith and Taffler's work (1995, 2000; see also Aerts, 1994; Sydserff and Weetman, 1999) has focused on the use of narrative and there has been extensive work on the use of graphical presentations (Beattie and Jones, 1997, 2001, 2002; Mather *et al.*, 1996, 2000). However, the most pertinent body of work as far as this current paper is concerned is that which has focused on the use of images in annual reports (Preston *et al.*, 1996; Graves *et al.*, 1996; McKinstry, 1996; Davison, 2004, 2007).

The majority of accounting research on the proliferation of visual and other sensual elements in the annual report has specifically focused on the use of photographs (Preston *et al.*, 1996; Graves *et al.*, 1996; McKinstry, 1996; Davison, 2004, 2007; Preston and Young, 2000). The recognition of the increased use of images in the accounts has been accompanied by speculation as to the purpose they serve, or rather how they "work". Graves *et al.* (1996) for example, found an increase in the use of images in the study of 14 US companies between 1949 and 1961. They suggested that these images perform a non-trivial function, arguing that they constitute an important part of the overall rhetoric or discourse of annual reports and as such support the truth claims contained within them (see also Rose, 2001). Preston and Young (2000), similarly suggested that the emergence of mediascapes within annual reports serve a constitutive function. In particular they focus on their role in the construction of corporations as global entities.

Of course the proliferation of images has not just been confined to the business reporting arena. Much has been written on the proliferation of the visual and what has been termed the ocular centrism of contemporary Western culture in general[1]. Within the accounting literature, the theorisation has focused on the social context within which this shift has emerged. McKinstry (1996) focused on the increased proliferation of design. He suggested that the increased use of visual images reflects the fact that annual reports are now worked on by graphic designers. Other research has focused specifically on exploring the relationship between the visualisation of annual reports, ways of knowing and constructed subjectivity. For example, in their US study, Graves *et al.* (1996, p. 62) focused on broader socio-cultural shifts in ways of knowing precipitated through the proliferation of television. They suggested that the changes in annual report formats reflect and reproduce cultural modalities and in this instance represent a broader shift towards the epistemology of television. In other words they reflected a cultural shift in ways of knowing and experiencing knowledge. They went on to say that, "their function is to persuade the report reader of the truth claims of the accounts and thus to perpetuate the values that reside in them". Preston *et al.* (1996) similarly focused on "ways of seeing" the images in annual accounting and outlined conventional/transparent, neo-Marxist and postmodernist examples. These perspectives were not so much presented as a list from which we are to choose, but an array of views that contribute towards our understanding of the reporting function and broader society. Preston and Young (2000) focused specifically on the way pictures and images are implicated and employed in the construction of corporations as global entities and how these representations reflexively construct the meaning of "global". Preston *et al.* (1996) concluded that current image work stifles the possibility of critical engagement, arguing that they encourage:

> [. . .] a way of seeing corporate images as inseparable from a vast visual apparatus in which the subject and reality have been constituted in the twentieth century. In this respect, images do not represent, they create reality. Critique is, thus, no longer a question of unmasking false representations of reality or ideology, but rather a question of both revealing and subverting the functioning of the collective apparatuses of subjectivity and reality production, of which mechanical reproduction and increasingly, the electronic production of images are part. It suggests an end to critiques based on binary oppositions (Preston *et al.*, 1996, p. 134).

Rose (2001), however, presented a less hegemonic view of images, contending that they can also act as sites of resistance. In the analysis that follows in section 3, we suggest a more dialectical view of the work of human faces.

Levinas, the face and Bauman

Within an entirely different stream of accounting ethics literature there is a small but growing discussion of the ethics of Emmanuel Levinas (Shearer, 2002; MacIntosh, 2004; Roberts, 2003; McKernan and Kosmala MacLullich, 2004) and also Zygmunt Bauman's sociological translation of Levinas' work[2] (McPhail, 2001; Funnell, 1998; Junge, 2001, Tester, 2002). We contend that there is a resonance between this emerging body of work and developments within corporate reporting, particularly in relation to representations of humans within these documents, and it is to this resonance that we now turn. We initially clarify our interpretation of Levinas's perspective then we explore Bauman's translation of Levinas's work into a form of sociological analysis (Tester, 2002). Finally, we draw on Bauman's sociology of adiaphorization (or disinterestedness) to clarify the interests of this paper.

According to Levinas, morality begins in the face to face. Similarly, Bauman argued that, "morality is the encounter with the Other as face" (Bauman, 1993, p. 48). And not only morality but I, myself, am constituted through my facing up to the Other (Bauman, 1993). Levinas commented:

> The absolute nakedness of a face, the absolute defenceless face, without covering, clothing or mask, is what opposes my power over it, my violence and opposes it in an absolute way, with an opposition which is opposition itself (cited in Bauman, 1993, p. 73).

These quotes establish a connection between Bauman and Levinas around the notion of the face. In this section we set out our understanding of the nature of this connection and the notion of the face.

The face is therefore fundamental to understanding Levinas's philosophy (and Bauman's sociology). However, as these quotes indicate, the idea of the face, like some other aspects of Levinas' writing, is less than transparent. Indeed, there has been some considerable debate about what he meant. Moran (2006, p. 347), for example, has noted that, "no term in Levinas' strange moral vocabulary has been subject to more analysis or given rise to more confusion [than that concerning the face]". Our understanding of the term commences from the observation that Levinas was a student of Edmund Husserl[3] and was thereby significantly influenced by his phenomenology (Moran, 2006).

We suggest that Levinas approached ethics from a radically different perspective from traditional moral philosophy. A major contribution of his work is that he approached ethics from a phenomenological perspective. For Levinas, ethics is not grounded in the questions, "what should I do?" or "why is it important that I behave in that way?" Where Husserl's phenomenological method involved asking, "what is the meaning of the thing as it presents itself to us?", so Levinas asked, "how does the experience of ethics present itself to us; what is the given-ness of ethics?" He concluded that it presents itself through *the Other*, through the encounter with the face; through the face to face. Levinas was therefore interested in the phenomenology of otherness and located the phenomenological given-ness of ethics in the relationship between myself and the Other. Part of the basis of this paper is therefore informed by Levinas' approach to ethics, in the sense that it provoked us to consider the phenomenological encounter with faces in annual reports and to question whether these encounters could be construed in any sense as ethical encounters within Levinas' terms.

We suggest that Levinas' position is grounded in consciousness and in particular on an implicit criticism of the Cartesian ego: *cogito ergo sum* ("I think therefore I am"). For Levinas, consciousness is always consciousness *of something*. It is "meaningfulness, thoughts casting themselves towards something that shows itself in them" (Levinas, 1993, p. 153). What this means is that a human being is not an, "isolated ego" (Moran, 2006, p. 328). Berger (1972, p. 1) similarly argues, "[s]eeing comes before words. The child looks and recognises before it can speak," and for Levinas, and many cognitive psychologists (see for example Gauthier *et al.*, 2000) the child's looking at faces plays a fundamental role in the development of individual subjectivity. As Moran (2006) said, it is the experience of an "I" that is not myself that is constitutive of my self. Moran (2006, p. 321) explained that for Levinas, "all social interaction is already in some sense taking place within the sphere of the other, the demand for ethics is always present, and as such it is an inescapable aspect of being human". Levinas' grounding of ethics in the phenomenology of otherness, is therefore a very different starting point from, for example, Rousseau, Locke, Hobbes and Hume. The beginning of ethics is not associated with my psychological preference for security, not my willingness to give up power to the State so that I can live in peace within a community. Rather, it is the way the face of the Other calls on me to curtail my power. Levinas' starting point is not what I get out of ethics, but rather the infinite claim it places upon me. He explained (in Bauman, 1993, p. 48), "In relation to the Face, what is affirmed is asymmetry; in the beginning, it does not matter who the other is in relation to me – that is his business". Moran (2006, p. 348) remarked, "The face stands in opposition to the will to be ... against the will to power ... We find ourselves addressed by the other". Each face communicates, saying, "Here I am," and in doing so it calls for justice. Moran (2006, p. 321) explained that for Levinas, the phenomenology of ethics involves, "the effort to constrain one's freedom and spontaneity in order to be open to the other person, or more precisely to allow oneself to be constrained by the other". That is its given-ness. Drawing on this interpretation of Levinas, we were provoked to further question the potential work of faces in annual reports in terms of the construction of the observer as a moral subject.

We therefore contend that Levinas employed the term "face" in both a literal and allegorical sense. He used it to refer to the literal encounter with another face. While it's easy to be deterred by Levinas's rhetoric, there is certainly evidence that the literal face-to-face does play an important role in consciousness and the development of neural networks[4]. Kaulingfreks and ten Bos (2007, p. 307) for example commented:

> The idea of the face is not simply based on eye contact, Yet, by choosing the face as an idea or concept that grounds ethics, Levinas clearly relies on some sort of ocular centrism. Again and again, Levinas makes clear how important the gaze is for it is the gaze that allows us to break through the form in which the other appears.

Moran (2006, p. 350) continued: However, Levinas also uses the term to refer to everything that evades objectification: for everything that evokes a willingness to serve the other for its own sake. There is a sense also in which the face to face is used to refer to more than a phenomenological description of how ethics presents itself to us. It is also an injunction. If I don't see something as having a face, it has no call on me and I have no responsibility towards it.There is therefore also a prescriptive element in Levinas's work that seems to be demanding us to see the face. Translating this perspective into the context of the annual report we then wonder whether the existence of faces in annual reports might be seen to represent a crowd of opportunities to be disrupted by the claims of others upon us. Yet the fact that this does not generally happen shouldn't be taken as self evident. As we shall contend below, when we consider the work of Bauman, in modern society, a lot of work goes into ensuring that we don't come face to face with the Other: that our encounter with the Other is not, in Levinas' terms, an ethical encounter.

Levinas' ethics is therefore quite fundamentally based on the phenomenology of the experience of the Other. While he employs the face in a literal way to refer to the conscious encounter with the Other, he also equates the face with ethics and asks that we ascribe the face to the Other. Having introduced Levinas' conception of face, we now want to turn to Bauman's sociological application of Levinas' work and in particular to the insights that he gives into the way in which individuals experience other faces within a modern social context. We find Bauman's work helpful precisely for the insights it provides into the observation that despite the proliferation of images of others' faces, they do not generally evoke a sense of responsibility. Bauman's application of Levinas is one way of thinking about why this might be the case.

Bauman's sociological translation of Levinas has appeared within the accounting literature specifically in relation to the Holocaust (see for example McPhail, 2001; Funnell, 1998). Bauman uses Levinas both to understand and to cope with his understanding of the Holocaust (Tester, 2002). First, drawing on Levinas, Bauman views the Holocaust not as an aberration, but as the clearest representation of modern society. Modernity's civilizing mission, contends Bauman, ultimately leads to Holocaust. He contends that it is the consequence of the administration of rules and laws enacted in order to enable individuals to live together. It occurs because the proximity of innate moral impulse (the face) is replaced by a legislative and bureaucratic relationship. Bauman therefore draws on Levinas in an analytical sense, in order to explain the Holocaust, but he also sees in Levinas a sense of hope. Tester (2002, p. 56) provides an example of the dual analytical and normative function of the presence of Levinas in Bauman's work. First, he explains, "his concern, following his study of the Holocaust was with the failure of the law. The law can't be depended on". However, he also alludes to the normative function that Levinas's ethics of alterity serves. Tester (2002) explains:

> Levinas is present in Bauman's work (and his presence is utterly incontrovertible) because he provides an escape from the pit of nihilism … The use of Levinas represents a kind of uncommon faith in humanity. At least uncommon in the sense of not being a common characteristic of sociological research.

It is important for the purpose of this paper and our analysis of human faces within annual accounts, to identify this dual analytical and normative helix.

The normative injunction is therefore necessary because, according to Bauman, the face has been dehumanised. He suggests that, within contemporary society, the encounter with the Other is managed to such an extent that the Other has lost its ethical claim. The face has been effaced in "a process similar to dehumanisation" (Bauman, 1993, p. 127). Tester (2002, pp. 68-69) explains further:

But as Bauman has also argued, social relationships and institutions mean that the possibility of any direct and undistorted relationship between the individual and the Other is either wholly dismantled (this is the nub of Bauman's sociology of adiaphorization); (Bauman, 1991) or mediated through social categories such as ethnicity, race, gender, religion, community and so forth (this explains Bauman's attack on communitarian politics and multiculturalism; Bauman, 1999, pp. xxxvi–xlv).

Junge (2001) makes a similar point when he says:

> It is the Face that calls forth my responsibility, and it calls it forth as Face, in its absolute alterity. The Other can never be "totalized", subsumed under some broader category such as "black", "brother in Christ", "Jew". It is the Face which has moral authority and nothing else. Such things as moral laws, reciprocity, particular human attributes have therefore no moral significance. Morally, they are nothing but dangerous distractions from the Face, irrelevancies which seek to subvert its absolute moral authority (cited in Woodhead, 1995, p. 22).

As Bauman states, acting according to an ethics of alterity means "facing the other as a face, not mask" (Bauman, 1995, p. 59). Finkielkraut (1997) outlines the possibility of the kind of point blank encounter, as opposed to the management of encounter[5], to which Bauman is referring. He comments:

> [. . .] when I encounter the other man face to face...his face lays claim to me. When mediation ceases to temper our relation, when his role, status, or the particular traits that delimit him no longer protect me from his presence, when he reveals himself to me *point blank*, the Other controls me with his weakness, immediately turning me into his debtor (Finkielkraut, 1997, p. 115).

Bauman (1995, p. 60) explained the uneasy consequences of being-for-the-other. He said:

> Once identified within the realm of being-for, the realm of morality is enclosed in the frame of sympathy, of the willingness to serve, to do good. To self-sacrifice for the sake of the Other.

These consequences seem entirely alien to an economic perspective based on the assumption of self interest. It is here that we wonder about the potentially paradoxical nature of the existence of faces within annual reports. Even if they are all symbolic of some other economic asset or accomplishment, why should it be important to us that they are symbolised in the face of others. Also, contrary to prevailing models of accountability, which are based on a responsibility-to, Bauman's modality of accounting involves a responsibility-for. Where the former is predicated on power, the power to hold to account, the later is based on pure weakness. Bauman (1995, p. 65) explains "one is responsible to someone stronger than oneself; one is responsible for someone weaker than oneself".

Thus, our reading of Levinas and Bauman provoked us to consider a number of issues relating to the phenomenological encounter with the face of others present within annual accounts. In particular we were concerned with three issues. Levinas's pre-ontological function of the face of Other; Bauman's discussion of the effacing of the Other in modern society; and finally Bauman's normative injunction to see the face of the Other. Our reading of Bauman and Levinas would therefore lead us to a three component interpretative model of the work of faces that we seek to bring to annual reports. First, the pre-ontological work of the face in establishing the self. Second, the defacing work of faces in the management of encounter. And finally, the potential work of the face as the basis of a normative ethical principle[6].

Having outlined both streams of literature that the paper attempts to combine, we are now in a position to more concisely summarise the primary concern of the paper. Firstly, as a matter of empirical curiosity, we wonder whether, given the significant changes in the nature, content and size of the annual reports, corporate reports contains more or fewer human faces over time. Having established an answer to this question of visual presence, we then draw on Levinas and Bauman to explore how these faces work. Drawing on Bauman's analytical perspective, we suggest that the presence of human faces in corporate annual reports may work towards the "dehumanization" of the Other (effectively suppressing ethics in Levinasian terms) and to the effacing of the fundamental ethical challenge that the Face of the Other poses to the reader. Yet, these faces are still potential faces and as such, the use of images of human faces in annual reports may paradoxically suggest that the supposed self-interested economic subject is in fact constituted in relation to the Other, thus supplanting the presumption of self-interest with a pre-ontological other-interestedness.

Within the accounting literature, Shearer (2002) suggested that conventional economic self-interest, represented the antithesis of Levinas' call to ascribe the face and be-for-the-other. Her work is in part a critique of Schweiker's (1993) argument that it is through the act of giving an account that moral identity (whether individual or organisational) is established. She claimed that while this may well be the case, if this observation were cast within the rubric of conventional economic thought, then the presumption that self-interested behaviour promotes society's interests as a whole would mitigate against the potentially disruptive nature of Schweiker's thesis. She concluded that (Shearer, 2002, p. 547), "identity as rendered in economic terms is insufficient to the task that Schweiker properly assigns it". In contrast to the self-interestedness of conventional economic theory, then, Levinas and Bauman present a radical Other-interestedness.

In the next section, we turn our focus to the representations of the human face in accounting documents.

3. Empirical method used in this study

From Bauman and Levinas' perspective, if the face of the Other is such a fundamentally important cognitive, moral and identity element, then it would seem at least plausible that as technological possibilities increase and as annual reports evolve in both size and complexity, then the face of the other might appear more readily within these documents[7]. The aim of this part of the paper is simply to establish the existence or non-existence of a trend to include faces within corporate annual reports, for further critical reflection rather than explaining why such a trend exists

Our sample comprised 14 companies that had been continuous members of the FTSE 100 since January 1988 for 15 years and that had not undergone any major change (by way of merger or demerger) that may have radically changed the management over that period. A starting-point of a date in the 1980s was selected because of McKinstry's (1996) observation that the introduction of design and the proliferation of images in the corporate annual reports can be traced to around the early 1980s[8]. The 1980s also seem to have been a significant decade in the visualisation of US annual reports (Preston *et al.*, 1996). Adams and McPhail (2004) and Campbell (2003, 2004) also found both frequency and volume of voluntary disclosures to have substantially increased around 1990[9].

The sample (which is shown in the Appendix) comprised 14 companies over 15 years, representing an analysis of 210 documents. Each annual report was studied for the occurrence of human faces[10]. Like Preston *et al.* (1996) we focused exclusively on photographs, although we accept (in fact we posit) that the interplay of text, photographs and other graphical images adds to the complexity of the representations of humans within the annual reports. Directors and company officers were discounted from the study as the disclosure of these forms is less discretionary than other faces[11]. In addition to the empirical data describing this trend, we also identified images used in a range of annual reports to illustrate the points made in the section 4 of this paper (Plate 2).

The results indicate, first, that there was a significant rise in human representation, in the form of the human face, during the period studied, as shown in Figure 1, a finding that is consistent with those of Graves *et al.* (1996) and McKinstry (1996).

From a sample of three companies in our sample over all years, we found that 76 per cent, 80 per cent and 90 per cent respectively, of the photographs they contained had humans in them.

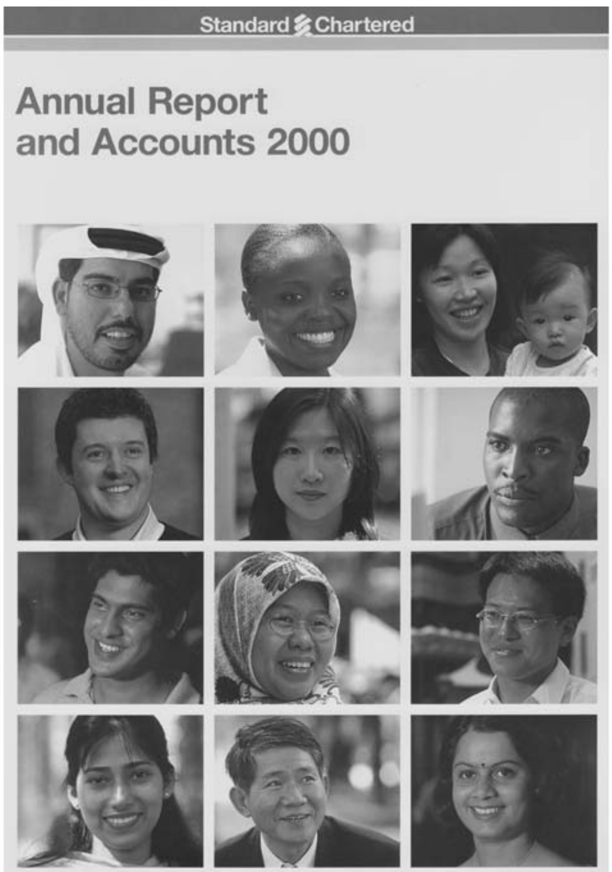

Plate 2.
Standard Chartered plc annual report cover, 2000

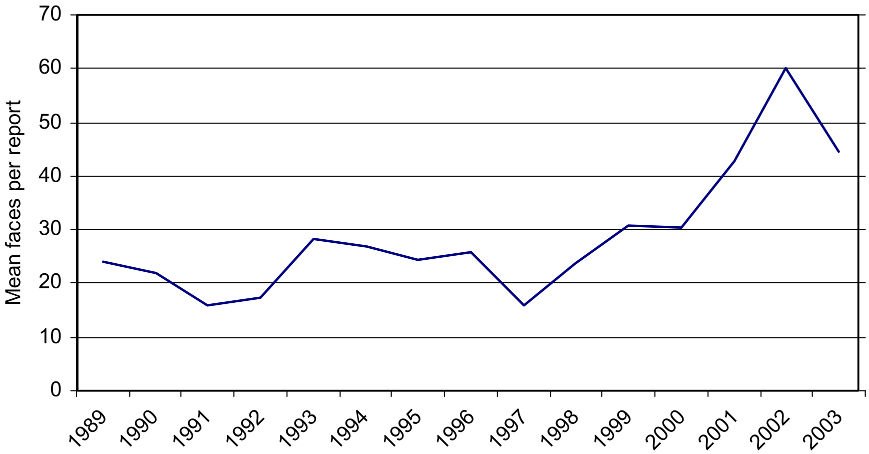

Figure 1.
Mean number of human faces, by year, in the annual reports of 14 FTSE companies (see Appendix 1)

4. Discussion

The findings suggest that with the proliferation of design and the increasing visualisation of corporate annual reports, there has been an increase in human representation within reports: male and female faces, young and old faces, faces of clients, managers, customers and employees. Drawing on our phenomenological interpretation of Levinas, combined with specific example pictures from annual reports, we begin to explore the work these faces may do in the encounter between the reader and the corporation that these Others represent. Our discussion initially draws on some contemporary visual methodology in order to deal with the fact that the encounter proceeds specifically through *pictures* of others. We then briefly address a second issue, namely that these pictures are anchored in the annual report.

Pictures of others and visual methodologies

Having described the theoretical basis of our study in Levinas and Bauman, and established the significant and growing presence of pictures of others in annual accounts, we now need to make the connection specifically between the others represented in the photographic images and the viewer, who remains outside these images. In other words we are required to determine the nature of the phenomenological encounter with the photographed other in particular.

Contemporary visual methodologies tend to split the analysis of images into three distinct arenas or "sites" of investigation (Rose, 2001): the site of production; the site of the image and finally, the site of audiencing (or focalisation) (Fisck, 1994). The site of production refers to the factors and motivations surrounding the creation of the image, the site of the image focuses exclusively on the content of the image itself (see for example Preston *et al.*, 1996). The third arena, the site of audiencing, focuses on the work images do in positioning the spectator (Fisck, 1994). Thus, informed by our reading of Levinas and Bauman above, we are interested in the way in which the image operates to position the "I" in relation to the Other. In this section we therefore focus on this third site in order to explore the extent to which human representation may be seen to operate in a powerful way within the accounting reports. We suggest that the images are powerful in the sense that they position the spectator in the encounter with the face of the (or an) other (Williamson, 1978) and that this, to some extent, shades the phenomenological encounter with the organisation.

The site of audiencing relates to the work that the image does on the viewer in positioning him or her in relation to the subject matter of the image. The image works to locate the audience within a particular set of relationships and, by inference, within a particular set of power relationships[12]. Berger (1972) for example, commented that the image never stands in isolation; it always includes the relationship between the image and the viewer. He explained thus:

> In the average European oil painting of the nude, the principal protagonist is never painted. He is the spectator in front of the painting and he is presumed to be a man. Everything is addressed to him. Everything must appear to be the result of his being there. It is for him that the figures have assumed their nudity (Berger, 1972, p. 48).

The image thus not only conveys something about the thing represented, it positions the viewer in relation to the image and in doing so, constructs the viewer. Here, we see traces of Levinas and Bauman's contentions relating to the Others' role in constructing the moral self. Rose (2001) has identified a number of sets of relationships involved in the image: the spectator, the image-maker (photographer or artist for example), the subject, and often, a commissioning agent. For example, she pointed out that in some circumstances, the image does not so much convey the feelings of the photographed, but rather, represents a submission to the feelings of the owner. Again, we see a resonance between Rose's visual theory and Bauman's notions of the defaced face of the Other. Rose quoted Berger (Rose, 2001, p. 14):

> Normally, it might be a Venus and Cupid. In fact it is a portrait of one of the king's [Charles II] mistresses, Nell Gwynne . . .(Her) nakedness is not, however, an expression of her own feelings; it is a sign of her submission to the owner's feelings. (The owner of both the woman and the painting.) The painting, when the king showed it to others, demonstrated this submission and his guests envied him (Berger, 1972, p. 52).

Any engagement with the faces contained within annual reports should therefore bear in mind the commissioning power behind the orchestration of the image and its presentation to the spectator. According to Rose, the spectator is therefore positioned not only in relation to the face in the image, but also in relation to the commissioning agent of the face. In this sense then, the faces may work to establish a relationship between the spectator and the commissioning agent, as well as the individual subject (see Plates 3 to 6).

Much of the work the image does on the spectator depends on the spatial organisation of the image (Rose, 2001). Bal (1996) focused on the range of different viewers implied in the composition of the picture, referring to the way the audience is managed and incorporated into different focal points in the picture as the number of different focalizations. Rose (2001) called this element, the "structure of looks".

A range of different focalisations are offered to the spectator within corporate reports. Plates 3 and 4 for example locate the viewer at the service provision end of the corporation, at the customer check-in desk in the case of Plate 3 and with an advisor, in the case of Plate 4. In both cases the spectator is not directly engaged by the individuals within the images. Contrast this observational positioning with the kind of direct engagement exhibited in Plates 5 and 6. In both cases, the spectator is directly engaged through both eye contact and the proffering of a product. Other images offer the viewer positions within the organisation. Plates 7 and 8, for

Plate 3.

Plate 4.

Plate 5.

Plate 6.

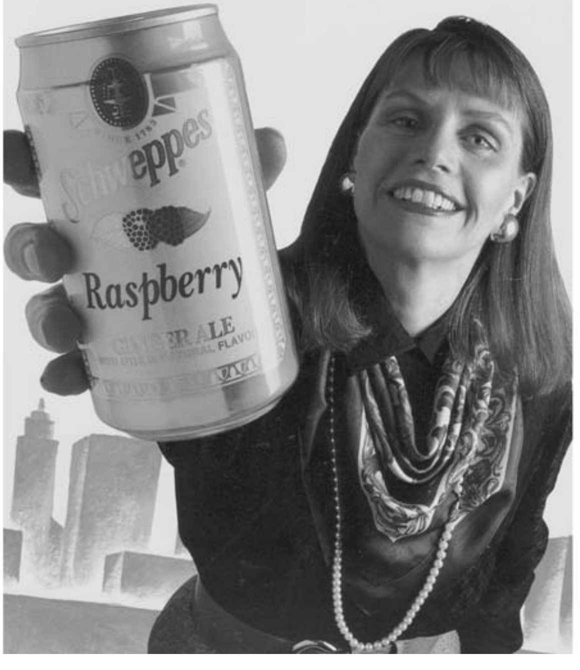

Plate 7.

Plate 8.

example position the spectator amongst the manufacturing and service functions within the organisation. These particular images also locate the spectator at different proximities to the subject (Kress and Van Leeuwen, 1996). In Plate 7, the viewer is located some distance from the subject, however in Plate 8 the spectator is positioned alongside the driver. Although Plate 8 contains only traces of the driver's presence, his hands and part of the side of his face, the viewer nevertheless occupies a more intimate position with the subject as opposed to simply looking at him. Plates 9 and 10 position the spectator with consumers of the corporation's services or products. Plates 11 and 12 position the viewer above the subjects and Plates 13 and 14 position the spectator with members of a community of others aided by the corporation's charitable giving (see Plates 7 to 10).

All these faces work on the reader, positioning them geometrically above, below or on the level, spatially close or distant, observing or participating. From our discussion of Bauman above, it seems quite clear that these encounters are mediated through social categories and roles. As Finkielkraut, (1997, p. 115) commented, it is only "when his role, status, or the particular traits that delimit him no longer protect me from his presence, when he reveals himself to me point blank, that the other controls me with his weakness". But these images do call for a response. They call for the spectators to accord themselves meaning in relation to these others, a meaning that may be different depending on the focalisation in question (see Plates 11 to 14). Williamson (1978, p. 41), writing with regard to advertisements, commented that:

> We [the advert viewer] must enter into the space between the signifier and the signified ... This space is that of the individual as subject: he or she is not a simple receiver but a creator

Plate 9.

Plate 10.

Plate 11.

Plate 12.

Plate 13.

Plate 14.

> of meaning. But the receiver is only a creator of meaning because she has been called upon to do so. As an advertisement speaks to us, we simultaneously create that speech (it means to us), and are created by it as its creators.

However, as we noted above, Bauman explained the ethical nature of one possible ascription of meaning from a Levinasian perspective:

> It will be only later, when I acknowledge the presence of the face as my responsibility, that both I and the neighbour acquire meanings: I am I who is responsible, he is he to whom I assign the right to make me responsible. It is in this creation of meaning of the Other, and thus also of myself, that my freedom, my ethical freedom, comes to be (Bauman, 1993, p. 86).

This is by no means an exhaustive list of the many different focalisations offered to readers of corporate reports, however they do provide some examples of the work that representations of human faces can accomplish in establishing an encounter between the spectator and others in pictures.

Pictures of Others in annual reports

However, as our discussion of Rose above highlighted, the spectator is also positioned in relation to the commissioning agent of the face. Given that the faces we have presented and discussed are broadly anchored[13] in the annual report, we conclude this section with some comments on the way faces may work on the spectator to presence them in relation to the corporation. As the expanding use of pictures presence the spectator, not just in relation to buildings, machinery and service, but also with other human beings, what is the impact of this face work in relation to the construction of the corporation in particular? While it is unlikely that the audiencing of any single image within an annual report will have a significant impact on the spectator's view of the corporation, perhaps taken together, the general increase in human representation within annual reports may work by gradual accretion on the spectator, placing them with other human beings and impacting the phenomenological encounter with the corporation.

One of the initial problems in speculating on the ethical impact of these faces is identifying the spectator. For example in Berger's discussion of the European nude above, the spectator could just as well be the king or his mistress as well as one of the king's consorts. It could therefore be the case, that the images serve the fantasies of the preparers of the reports, enabling them to re-affirm their own self-conceptions of and to themselves (Roberts, 2003). Or they could be for the investor's benefit, providing them with an opportunity to project their own fantasies into their investment practices. Are these faces reassurance that what they are doing helps their fellow human beings? A psychological need that does not sit well with the economic focus on self interest and the individual, unless it is intended to provide a reassurance that the pursuit of self interest does have positive social consequences (Schweiker, 1993; Shearer, 2002). Drawing on the intellectual capital literature, it might be possible to explain some of the increase in human representation of employees as an attempt to signal the existence of a form of human capital not captured by conventional accounting reporting mechanisms (Sveiby, 1997; Wexler, 2002; Pedrini, 2007). However, this explanation does not easily apply to the many different kinds of faces depicted, including the picture of the young child on the title page (Plate 1). Either way, we contend that the increased use of human faces in corporate accounts is at variance with mainstream economic moral psychology. "Others' really shouldn't matter that much. We agree with Schweiker (1993) and Shearer (2002) that the act of rendering an account is constitutive of the moral self and that corporate annual reports represent a paradoxical aberration that confirms that self-interest is not enough. However, we contend that not only the act of rendering an account but also the increasing humanisation of the visualised medium through which accountability is discharged is similarly paradoxical. The increased aesthetisisation of the corporate report, and in particular the increased use of human faces is, as Levinas might say, evidence that the Other is already under our skin.

Yet while the presence of so many Others in the annual report may hint towards the pre-ontoloical importance of the Other for our own being (Moran, 2006), these faces seem to evoke a phenomenology of consolation and reassurance, rather than self-sacrifice (Bauman, 1993). The economic logic of corporate reporting would certainly imply that the face to face is not perceived to be threatening[14] (Bauman, 1995). In other words, the use of faces in annual reports conveys something about the kind of moral society we live in and the way encounters with the other are mediated within different contexts and made bearable (Bauman, 1995): a morally reassuring but not disruptive presence. They are faces that have no moral glare, effaced faces that lie beyond moral impulse (Bauman, 1993). They have been categorised as customer, van driver and consumer, and in the process morally de-signed – all of which Bauman sees as part of the bureaucratic effacing of the Other. In Bauman's terms, the corporate report, now with its many images of other people, is part of the bureaucratic technology that stops people seeing each other.

Bauman (1995) for example, contends that we live in an era of the anonymous, where relationships with Others are not possible, an epoch of being-with, rather than being-for. It's easy to encounter them in print, but not to see the face. As Moran (2006, p. 350) commented: "if I don't see something as having a face, it has no call on me and I have no responsibility towards it".

But they do remain potential faces. Here we seek to make a connection with Bauman's second, normative and hopeful invocation of Levinas. They do provide an opportunity to "escape from the pit of nihilism" (Tester, 2002, p. 56). All that is required to turn them into faces is a reader-prepared-to-see-them, and an "uncommon faith in humanity" (Tester, 2002). To some extent, all of this corporate representation of humans in annual reports gets in the way of the most fundamental piece of work that the face of the Other can do: constituting the spectator as a moral self (Levinas). Every Other says "here I am". But it is the responsibility of the "observing subject" (Preston *et al.*, 1996), to see them. It is my responsibility to confront the Other as a face (Bauman, 1993). It is my positioning her as the face that is a moral act; the moral act (Bauman, 1993). According to Levinas it is in the taking of this responsibility that I find my being. This face works to bring the spectator into moral being. The faces are there, but what is required is an awakening to the face (Bauman, 1995). Kaulingfreks and ten Bos (2007, p. 307) commented:

> It is the way that someone looks us in the eye that allows us to break through the form in which the other appears. The eyes are absolutely naked and in the vulnerability of this nakedness, in its unmasked non-presence, the face gets its meaning or its expression. The face is therefore an expression, not of an idea or an image, but of what is as such ("kat'auto"). It is not a thing ("tode ti") that can be understood in a system of knowledge or in a system of relations. Its expression is rather an invitation to be with, to live with him or her, to be put in a society ("societe") with him or her.

It is here that we challenge Shearer's (2002) application of Levinas to the possibility of corporate identity. This would seem to us to be counterintuitive to Levinas's critique of established theorisations of social ethics for example in Hobbes, that are based on reciprocal obligations (McKernan and Kosmala MacLullich, 2004; Roberts, 2003). On the contrary, we contend that Levinas represents a challenge to the idea of a unitary corporate identity. It is the fact that the corporation is composed of different human beings (as a society of faces), as is perhaps unintentionally implied through the images, that presents the crux of Levinas's moral challenge. According to Levinas, morality rests in the specificity of the individual Other. When the individual dissolves into the crowd of society, or for that matter, corporate identity, morality dissolves with them (McKernan and Kosmala MacLullich, 2004). The fact of the matter is that while corporations have an image, they do not have a face, certainly not in Levinasian terms. They do, however, consist of faces and it is here that the increased use of faces represents a further ethical challenge. They represent individuals (others) that, within the corporation, investors and so on, need to care for, or be for, if their being is to have any ethical justification at all (Moran, 2006).

5. Conclusion

Our intention in this paper was to draw on the work of Emmanuel Levinas and Zygmunt Bauman in order to explore two related questions. First, to what extent do corporations use images of human faces in their annual reports? And second, how do these images "work"? We studied human representation in the annual accounts of 14 FTSE top 100 companies, for the 15 year period from 1989 to 2003 and found first, that there was a significant rise in human representation in the form of the human face over the period of the study. In our subsequent discussion of this finding, we drew on some critical visual studies literature in order to explore the nature of the work accomplished specifically by pictures of faces in the positioning of spectators. We then proceed to engage with the final step in our analysis: the anchoring of these images within the annual reports in particular. During both steps in our discussion we provide some broader reflections based on our reading of Levinas and Bauman and in particular Levinas' pre-ontological function of the face of Other; Bauman's discussion of the effacing of the Other in modern society; and finally Bauman's normative injunction to see the face of the Other.

We suggested that the presence of human faces in corporate annual reports may work towards the "dehumanisation" of the Other (effectively suppressing ethics in Levinasian terms) and to the effacing of the fundamental ethical challenge that the Face of the Other poses to the reader. Yet, these faces are still potential faces and as such, the use of images of human faces in annual reports may paradoxically suggest that the supposed self-interested economic subject is in fact constituted in relation to the Other, thus supplanting the presumption of self-interest with a pre-ontological other-interestedness.

Notes

1. Note however that the visual has not developed in isolation to the discursive. The increasing visualisation of Nike, for example, has happened in conjunction with opportunities to "talk to" Nike via the web. Also, Rose (2001) suggests that there is some considerable debate as to the accuracy of the claim that visualisation is something new. She contends that the visual has always been culturally important
2. Bauman's interpretation of Levinas is not uncontested. For a brief critique of Bauman's interpretation of Levinas see Abbinnett (1998).
3. 1859-1938, sometimes referred to as the "father of phenomenology".
4. Within neuroscience the brain is considered to play an important role in conveying important social information. Neuroscience would suggest that neurological processes relating to face perception can be identified even at birth. In fact, if the specific part of the brain that process information about faces is damaged in some way, this can result in a neurological condition known as prosopagnosia which roughly translates as face blindness. Neurological science suggests that human beings have an innate predisposition to pay attention to faces (see for example Gauthier *et al.*, 2000).
5. Levinas similarly employed the term 'management of encounter' to refer to the removal of the possibility of encountering the other and with it, any associated obligations. This, according to Levinas is not just a likely outcome of economic calculation; it is a cultural form.
6. It may be helpful here to construe "the face of the Other" as being akin to Kant's categorical imperative or Rawls's original position. The face of the Other is a normative position that is of course fundamentally different to, for example, Rawls's administration of justice, however it is about what must be done.
7. Of course there may be other explanations for the emergence of human representation within accounts. For example, the discourse of intellectual capital may be accompanied by greater human presence in the annual reports as companies endeavour to convey the existence of

human or customer capital. As we explain below, we attempted to identify a range of images that might help us to ascertain whether this may be at least as plausible an explanation for any trends identified.

8. McKinstry (1996) suggested that Burton's first used images in its 1981 report. He suggests that while this represents one of the earliest examples of design impacting on company annual reports in the UK, the use of images did not emerge as a conscious strategy in Burtons accounts until 1984 and that other companies followed only later.
9. Although Graves *et al.* (1996) found evidence of the use of pictures as early as 1917 in the reports of US companies and noticed a specific increase around the 1940s.
10. We defined a face as a full or partial human face as viewed from a number of different angles, for example side on and face-to-face. All occurrences were combined. Our statistics do not differentiate between for example different perspectives or different proximities, in the sense of a near face and a far face.
11. Our decision to exclude pictures of directors was related to our endeavor to identify the (non) existence of a reporting trend. These, predominantly old, male, white faces undoubtedly do work, and could be the subject of an interesting study in itself. However, as we were primarily concerned with manifestations of the extent to which the Other is, "already under our skin," to employ Levinas' we focused on voluntarily produced images of others.
12. Very often the process of making meaning, depends on some prior "code". Rose (2001) made the point that making sense of some of the signs requires a wider set of conventional meanings. These are often associated with particular groups of people and the way these groups make meaning. For example advertising companies develop adverts that are informed by and require the individuals seeing the images to be working with a certain set of codes. These require some prior encoding. We need to know, for example, that a certain person is beautiful. These codes give us access to particular ideologies according to Hall (1980). Hall (1980) referred to these as ideologies as meta-codes.
13. The anchorage of the image is important and provides help with deciding between competing different meanings. Anchorage is often provided by text.
14. It would seem unlikely that faces on individuals would be included if they thought these faces would undermine the corporation's legitimacy.

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Appendix 1. Sample

- Insurance and related – Legal and General.
- Banks – Royal Bank of Scotland; Standard Chartered.
- Defence and related – BAe systems; GKN.
- Property – Land Securities.
- Food and Drink – Cadbury Schweppes; Allied Domecq.
- Retail – Boots.
- Medical equipment – Smith and Nephew.
- Engineering – Rolls Royce.
- Media – Granada.
- Publishing – Pearson; Reed Elsevier.

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Appendix 3

Slack, R. (2006) *British Accounting Review*, 38 (1), pp. 125-127, Review of Morrow, S. (2005) *The business of football, image management in narrative communication*, The Institute of Chartered Accountants of Scotland, Edinburgh read for researchers interested in financial reporting, capital markets and corporate governance.

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Stephen Morrow, The business of football: image management in narrative communication (2005, Institute of Chartered Accountants of Scotland, Edinburgh) 72 pages

The author of this research monograph is well known to readers of texts and journal articles on the football industry and its changing financial and societal position (see for example Morrow, 1999, 2003). The reviewer was not surprised, therefore, to find extensive contemporary literature coverage in the monograph on the broad area of research in football. This is complemented by a substantial literature review on content analysis, this being the prominent research method employed for the study.

The study is an interesting application of content analysis where the voluntary disclosure narrative in annual reports of football clubs in England and Scotland is studied. Noting an increase over time, the study suggests that a desire by football club management to portray a more positive image may be the cause. This, of course, leads to a fundamental question as to why football as a sector needs to manage its image and what issues might cause a potential image problem. This question is addressed through a discussion contrasting the financial and football related objectives that face football club managements and their relationships with a broad stakeholder base that includes supporters, local communities and the environment. In order to manage some stakeholders or to divert attention away from poor financial performance (caused in part by excessive wages) it is argued that a more positive image can be 'spun' within the voluntary narrative.

Two fundamental questions need to be asked as a follow up to this. Firstly, are stakeholders (for example, supporters) really concerned with (or even aware of) poor financial performance and wage levels? If they are not, then for whom are such voluntary disclosures intended? Are supporters of Newcastle and Liverpool concerned over the combined wages of Messrs Owen and Gerard for example? Secondly, and a major research method issue in this context, is the use of the annual report as the sole document for analysis justified. The study could be developed by a discussion on the usefulness of other sources of official and unofficial information such as the club website, supporter websites or fanzines. If the increased voluntary disclosure is a way of managing image to stakeholders, are we sure that these intended recipients read the annual report or can the increase in disclosure be explained by other factors such as mimetic behaviour across the sector? So while an interesting question about image management by voluntary disclosure is raised, can we be sure that this question can be fully answered by this research?

The study employs both quantitative and qualitative elements of content analysis, the latter being concerned with news direction of disclosure and categorised as good, neutral or bad. The study clearly shows that the majority of reporting is either good or neutral news with less than 15% being bad news disclosure. However, given that football club directors/management write their own voluntary disclosure, these results are probably not surprising. Management can thus portray a positive reflection of their club and relegate any voluntary bad news out of the annual report.

The method part of the report covers coding and the use of inter-coder agreement and this increases the reliability of the content analysis findings. Readers new to content analysis would benefit from a study of this section and the supporting references used as they provide a good introduction to the subject. The selection of the clubs used in the study comprised a sample of English and Scottish Premier League clubs for all years from 1997/1998 to 2001/2002. This method of selection raises issues in respect of the consistency of sample membership. As clubs enter and leave the divisions being studied, by relegation and promotion, the continuity of clubs within the Premier Leagues (England and Scotland) that comprise the sample changes year on year. The level of voluntary disclosure (and thus image management) may be influenced by this factor and thus may distort the results. This potential distortion would be avoided if all the clubs in the sample had remained as constant members of their respective leagues over the five-year study. A further issue is raised by the inclusion of both stock exchange listed and non-listed clubs in the sample. The contention made in the monograph that listing status confers visibility, for example, is challengeable. West Bromwich Albion and Charlton Athletic are listed whereas Liverpool and Everton are not.

The two-country study highlighted some interesting national differences. While voluntary narrative has increased over time in both countries, the English clubs have consistently disclosed more voluntary narrative than Scottish clubs.

The results and analysis are neatly presented with appropriate graphical support and the use of two small case studies. It was curious, given the otherwise complex presentation of findings that more was not made of the earlier discussion on image management as a prominent motive in voluntary disclosure. The foreword asserts "as many supporters do not have expertise in interpreting financial statements, a large part of the communication burden falls to the narrative reporting of the annual report." Whereas readers might expect a clear link back to these stakeholder image management issues at the findings stage, the monograph instead proceeds to a detailed discussion on the variables covered in the voluntary reporting, not always noting how these issues might affect relevant stakeholder groups as it does for instance with regard to player acquisitions. A more interesting and thought provoking approach would have been for all of the reporting variables to be considered in the context of stakeholder image management.

Overall, however, the text is an interesting and well-referenced read, providing as it does, a useful extension to the content analysis literature and a good discussion of the issues of the ascendancy of profit over the stakeholder claims on businesses within a sector. Using annual reports however can be a two edged sword: good for availability and a public record but how reliable are they as a research document employed to measure stakeholder image management?

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Appendix 4

Slack, R. (2009), ‘A lack of interest’, *Environmental Finance,* June, p.29.

A lack of interest?

Given the banking sector's fundamental role in the global economy and the fundamental economic threats posed by environmental issues, equity analysts covering the sector might be expected to care about banks' environmental reporting. Not so, found **Richard Slack**

Watching the financials – but equity analysts aren't looking out for environmental exposures

A growing number of corporations, in their reporting to shareholders and the wider public, devote pages of information to their environmental footprint, environmental management and sustainability strategies, whether as part of their annual reports or as specific stand-alone social and environmental publications.

Meanwhile, there is a growing appreciation that the management by companies of social and environmental issues can be material to their financial performance, or provide a proxy for the overall quality of their management. How investors, and the analysts upon which they depend, use these company disclosures should be an important consideration both for the companies producing this information and for those seeking a wider understanding of how the financial markets are responding to social and environmental issues.

Much academic research in this area has focused on 'dirty industries' such as oil, mining and petrochemicals. In terms of its environmental footprint, the banking sector is normally viewed as relatively clean. However, while banks' direct operations may be relatively low-impact, they are complicit through their lending to the environmental footprints of their clients – and are potentially exposed to both reputational risk and direct losses from poor environmental management by their customers (see *Environmental Finance*, March 2009, pages 24–25).

Against this backdrop of environmental risk within the banking sector, qualitative research – funded by the Association of Chartered Certified Accountants – was carried out by myself and David Campbell of Newcastle University in the UK. We sought to examine the views of equity analysts covering the UK banking sector towards banks' environmental disclosures in their annual reports, and the analysts' general attitudes to environmental risk and reporting.

If the climate change agenda is a deep-rooted concern, then it might be expected that capital market participants, such as analysts, would be well positioned to comment on the financial consequences of environmental risk and would use this as a factor in forming their opinions on banks in the sector. The analysts may also be influential in enhancing environmental reporting by banks in response to their needs – for instance, by providing more granular information on loan book environmental risks.

The research involved interviewing 19 UK retail bank analysts at so-called 'mainstream' financial institutions (excluding specialist socially responsible investment analysts) prior to the current financial crisis. Given this period of bank growth and relative calm in the financial markets, the views and mindsets of the analysts are particularly revealing about the materiality and relevance of non-financial aspects of bank performance and reporting.

Overall, the analysts' views on environmental issues ranged from the cynical to the outright dismissive, with environmental disclosures made by banks rarely read. The focus of analysts was largely confined to accounting numbers, financial information and performance with scant regard to wider factors. This attitude was commonly held across our sample, and potentially signifies an institutional culture with a rigid focus based upon accounting numbers and financial performance to the exclusion of other wider and potentially more challenging longer-term issues, facing not just banks but global companies as a whole.

Bearing in mind the pivotal role played by banks through financing, this lack of concern, and perhaps ignorance, about environmental issues is curious to say the least. In answer to the question concerning potential bank reputation risk over environmental issues, one analyst replied that: "if it was like a nuclear power station or an oil company I might worry about it a bit more". At a more general level, the attitude towards social and environmental reporting was encapsulated by the following two responses: "social and environmental report – absolutely useless from my point of view" and "environmental blah blah blah blah. It's a bank."

Our research clearly shows that bank environmental reporting and bank-related environmental risk factors are apparently universally considered irrelevant by bank analysts. Furthermore, the findings show that analysts were dismissive of anything other than financial metrics. In general, the analysts were shown to be narrow in their approach, often formulaic and rules-driven, and highly unlikely to be a source of change in respect of social and environmental issues. It may be that the current financial crisis will lead to a re-appraisal of wider, non-financial factors by analysts. This may be particularly true in respect of risk and governance aspects of performance and reporting, as these two factors lie at the heart of the current situation. If so, will the same wider re-evaluation and reflection also apply to environmental considerations and the role played by banks and the provision of finance?

Alternatively, the financial nature of the crisis may simply serve further to harden attitudes that financial considerations and performance dominate above all else, leading to wider and longer-term issues such as the environment continuing to be ignored or deemed not material or relevant. Such an outcome should be a major concern to wider market participants, given analysts' crucial role in the information supply chain.

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